Supreme Court U.S.
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No. ___

IN THE SUPREME COURT
OF THE UNITED STATES

GORDON DAVENPORT,
Petitioner,

v.

UNITED STATES OF AMERICA,
Respondent.

ON PETITION FOR A WRIT OF CERTIORARI
TO THE UNITED STATES COURT OF APPEALS
FOR THE FIFTH CIRCUIT

PETITION FOR A WRIT OF CERTIORARI

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QUESTION PRESENTED

An estate filed suit in tax court under 26 U.S.C. § 6213 to contest an alleged gift tax deficiency on the ground that no completed gift occurred during the tax period. For purposes of the tax court proceeding only, the estate and the Government stipulated the value of the property allegedly constituting the gift. The tax court ruled that a completed gift occurred during the tax period and that the estate owed gift tax based on the stipulated value. Thereafter, the Government sued the alleged transferee of the gift, seeking to hold him liable for the unpaid gift tax under 26 U.S.C. § 6324(b), which limits the amount of transferee liability to the value of the property transferred.

The question presented, on which the courts of appeals are divided, is as follows:

Whether the Government may rely on the res judicata effect of the tax court adjudication to establish elements of the § 6324 claim, including the alleged transferee's status as a transferee and the value of the property transferred, even though (1) the alleged transferee was not and could not have been a party to the tax court proceeding and (2) the Government has the burden of proof on these elements in the § 6324 proceeding, but the estate had the burden of proof in the tax court proceeding.

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PETITION FOR A WRIT OF CERTIORARI

Gordon E. Davenport respectfully petitions for a writ of certiorari to review the judgment of the United States Court of Appeals for the Fifth Circuit in this case.

OPINIONS BELOW

The April 9, 2007 opinion of the Fifth Circuit Court of Appeals reversing the judgment of the district court (App. 1a-17a) is reported at 484 F.3d 321. The Fifth Circuit's May 14, 2007 order denying Petitioner Gordon E. Davenport's petitions for panel and en banc rehearing (App. 85a-86a) is unreported.

The district court's June 18, 2004 opinion and order granting in part and denying in part Mr. Davenport's Motion for Summary Judgment and the Government's Cross-Motion for Partial Summary Judgment (App. 18a-39a) is reported at 327 F. Supp. 2d 725. R.757.[1] The magistrate judge's February 22, 2005 report and recommendation that the district court grant in part and deny in part Mr. Davenport's Second Motion for Summary Judgment and the Government's Second Cross-Motion for Partial Summary Judgment Regarding Valuation (App. 40a-50a) is unreported. R.1027. The district court's March 16, 2005 order overruling the parties' objections to the magistrate judge's February 22, 2005 report and recommendation (App. 51a-52a) is unreported. R.1079.

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[1] The clerk's record is cited herein with the abbreviation "R." followed by the page range cited.

The magistrate judge's January 18, 2006 opinion and order granting Mr. Davenport's Third Motion for Summary Judgment (App. 53a-56a) is unreported. R.1726. The January 18, 2006 final judgment entered by the magistrate judge (App. 57a) is unreported. R.1729.

JURISDICTION

The judgment of the court of appeals was entered on April 9, 2007. Mr. Davenport timely filed petitions for panel and en banc rehearing on April 23, 2007. The court of appeals denied Mr. Davenport's petitions on May 14, 2007. The jurisdiction of this Court is invoked under 28 U.S.C. § 1254(1).

RELEVANT CONSTITUTIONAL AND STATUTORY PROVISIONS

The question presented implicates the following provision of the United States Constitution:

U.S. Const. art. I, § 8, cl. 1:

> The Congress shall have Power to lay and collect Taxes, Duties, Imposts and Excises, to pay the Debts and provide for the common Defence and general Welfare of the United States; but all Duties, Imposts and Excises shall be uniform throughout the United States . . . .

The question presented implicates the following provisions of the United States Code:

26 U.S.C. § 6324 (b):

> **Lien for gift tax.**—Except as otherwise provided in subsection (c), unless the gift tax imposed by chapter 12 is sooner paid in full or becomes unenforceable by reason of lapse of time, such tax shall be a lien upon all gifts made during the period for which the return was filed, for 10 years from the date the gifts are made. If the tax is not paid when due, the donee of any gift shall be personally liable for such tax to the extent of the value of such gift. . . .

26 U.S.C. § 6902(a):

> **Burden of proof.**—In proceedings before the Tax Court the burden of proof shall be upon the Secretary to show that a petitioner is liable as a transferee of property of a taxpayer, but not to show that the taxpayer was liable for the tax.

STATEMENT

This case presents the issue of whether the Government may rely upon the res judicata effect of a prior tax court adjudication of a transferor's tax liability, which was based on stipulated facts, to preclude litigation of discrete elements of a § 6324 transferee liability claim the Government subsequently asserts against an alleged transferee. The

Fifth Circuit concluded that the Government may do so, even though (1) the alleged transferee was not and could not have been a party to the tax court proceeding, (2) the factual elements in question were stipulated rather than litigated in the tax court proceeding, and (3) the Tax Code allocates the burden of proof on the elements to the Government in the § 6324 proceeding but to the transferor in the tax court proceeding.

The Fifth Circuit's holding, which constitutes a fundamental misapplication of principles of claim and issue preclusion articulated by this Court, creates a split among the circuits. Apart from the Fifth Circuit, courts have uniformly held that res judicata precludes a § 6324 defendant from litigating *only* the transferor's tax liability, but *not* other elements of the § 6324 claim. The Fifth Circuit's application of res judicata also eviscerates the Tax Code's allocation of the burden of proof to the Government in transferee liability proceedings, allowing the Government to rely on factual findings from a tax court proceeding in which the Government *does not* bear the burden of proof to establish factual issues in a subsequent transferee liability proceeding in which the Government *does* bear the burden of proof. Absent correction by this Court, the Fifth Circuit's holding in this case will undermine uniform application of the Tax Code, which is both constitutionally and congressionally mandated.

A. The Transfers.

Birnie Davenport and her sister Elizabeth Davenport jointly owned 3220 shares of stock in Hondo Drilling Company. R.833. While the sisters had orally agreed that they each owned half the stock, legal title to all of the shares was in Elizabeth's name. R.833. Elizabeth died in December 1979. R.832. In July 1980, Birnie transferred her interest in 1610 shares of the stock to her two nephews, Charles Botefuhr and Petitioner Gordon Davenport, and her niece, Patricia Vestal, in essentially equal amounts, using two conveyance methods.

First, Birnie transferred her interest in 537 shares to Mr. Davenport and 536 shares to Vestal through installment sale agreements that valued the stock at $804 per share. R.835.[2] The $804 price per share was determined by reference to Hondo's annual financial statement and its internal determination of the redemption price it was willing to pay shareholders to redeem their shares for the fiscal year ended August 31, 1980. R.834. Second, Birnie transferred 537 shares to Botefuhr as an outright gift. R.832. In a signed agreement, Botefuhr promised to file a gift tax return reporting Birnie's gift to

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[2] Birnie reported the installment sales on her 1980 income tax return and indicated on that form that the sales were to related parties. R.812. Copies of the sales agreements and Birnie's 1980 income tax return were provided to the IRS agent who later examined Elizabeth's estate. R.668. In March 1982, Birnie forgave the promissory notes Mr. Davenport and Vestal executed in connection with the installment agreements and timely filed a gift tax return reflecting forgiveness of the notes. R.835-36.

him and to pay on her behalf the gift taxes associated with his gift. Botefuhr did not fulfill this responsibility. R.814-16.

At the time of these transfers in 1980, it was anticipated that the IRS would dispute Birnie's ownership interest in the stock. True to predictions, in connection with an audit of Elizabeth's estate tax return, which listed among her estate's assets only 1610 shares of Hondo stock, the IRS took the position in 1982 that Elizabeth owned all 3220 shares of stock and that Birnie owned none. R.834. The ensuing litigation ultimately settled in 1984, when the IRS acquiesced in the estate's position that Birnie owned half of the shares in exchange for the estate's agreement to value the 1610 shares at $2400 per share as of the time of Elizabeth's death in 1979. R.834.[3] Because Birnie's ownership interest in the stock was in dispute at the time of the 1980 transfers, the value of what she transferred to her niece and nephews at that time was "speculative and subjective." R.1209.

B. The Gift Tax Deficiency and Tax Court Proceedings.

Birnie died in 1991. R.831. During the course of preparing her estate tax return, it came to light that Botefuhr had never filed the 1980 gift tax re-

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[3] Internal memoranda from the IRS acknowledge that the $2400 per share value was higher than the value of the stock the tax court would likely find and resulted more from the IRS's effort to settle the ownership issue than an actual market valuation of the stock. R.1711.

turn or paid the applicable gift taxes on his gift as promised. R.752. In November 1991, Birnie's estate filed the estate tax return and a gift tax return, reporting the 1980 gift to Botefuhr at $804 per share and paying gift tax of $95,322 with the return. R.832

In 1992, the IRS audited Birnie's estate tax return and 1980 gift tax return and claimed that (1) Birnie's gift to Botefuhr should have been valued at $2730 per share rather than $804 per share and (2) the 1980 sales to Mr. Davenport and Vestal constituted imputed gifts of $1861 per share because the stock was undervalued at $804 per share in the installment agreements. R.837, 1424. Birnie's estate filed suit in tax court under 26 U.S.C. § 6213 to contest the alleged resulting gift tax deficiency, arguing principally that Birnie did not make a completed gift in the third quarter of 1980 because she did not have legal title to the stock at that time and was not listed as record owner of the stock on Hondo's books. *Estate of Davenport v. Comm'r*, 74 T.C.M. (CCH) 405 (1997). Prior to trial, the Government and the estate entered into the following stipulation:

> *For the purposes of this litigation*, if the Court finds that Birnie Davenport transferred Hondo stock to Patricia Vestal, Gordon Davenport and Charles Botefuhr in the calendar quarter ended September 30, 1980, the parties agree that the fair market value of such Hondo stock was $2,000.00 per share at the time of the transfers.

R.837 (emphasis added). Notably, of the forty-four stipulations in the tax court, this constituted *the only one* that contained this limiting language. R.830-38.

The tax court concluded that, although Birnie did not possess legal title to the Hondo stock at the time, Birnie had completed transfers of her inchoate interest in the stock in 1980. App. 82a. Utilizing the parties' stipulated value for the stock, the tax court calculated that the estate owed $822,653.00 in unpaid gift tax. App. 5a. The estate appealed, and the Tenth Circuit affirmed. *See Estate of Davenport v. Comm'r*, 184 F.3d 1176 (10th Cir. 1999).

C. The Transferee Liability Proceedings.

In March 1998, the IRS made an assessment against Birnie's estate, but the estate lacked funds to pay the assessment, which, with eighteen years of penalties and interest, had ballooned to $5.2 million. R.703. In February 2000, the Government filed the current action in the Northern District of Oklahoma, seeking to hold Mr. Davenport, Vestal, and Botefuhr personally liable for the unpaid gift tax as transferees under 26 U.S.C. § 6324(b). R.23.[4] The Oklahoma district court, after denying Mr. Davenport's and Botefuhr's motions to dismiss for lack of per-

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[4] The Government also named Birnie's estate as an additional defendant in the action, seeking to reduce to judgment the tax court's adjudication of Birnie's tax liability through a separate count from the § 6324(b) claims asserted against the remaining defendants. R.23, 25-27.

sonal jurisdiction, granted summary judgment for the Government on its § 6324(b) claims against all three cousins. *See United States v. Estate of Davenport*, 159 F. Supp. 2d 1330 (N.D. Okla. 2001).

On appeal, the Tenth Circuit held that the district court lacked personal jurisdiction over Mr. Davenport and Botefuhr. *See United States v. Botefuhr*, 309 F.3d 1263, 1274 (10th Cir. 2002) (Ebel, J.). In considering Vestal's appeal of the summary judgment against her, the court held that the district court erred in holding that Vestal was bound by the tax court stipulation as to the value of the stock she received from Birnie. *See id.* at 1281-82. Specifically, the court held that (1) collateral estoppel, rather than res judicata, governed the determination of whether Vestal could litigate the value of the stock interest she received from Birnie for purposes of determining the scope of her § 6324 transferee liability, and (2) because the stock value had been stipulated rather than actually litigated in the tax court proceeding against Birnie's estate, collateral estoppel did not preclude Vestal from litigating the valuation issue. *See id.* at 1282-83.

On remand, the Government's case against Mr. Davenport was transferred to the Southern District of Texas. R.548. The parties filed cross-motions for summary judgment on numerous matters, including the preclusive effect of the tax court proceeding. The Government argued that res judicata prevented Mr. Davenport from litigating Birnie's tax liability and that collateral estoppel pre-

vented him from litigating the valuation issue.[5] R.946-60. Like the Tenth Circuit, the district court rejected the Government's argument that collateral estoppel prevented Mr. Davenport from contesting the value of the inchoate stock interest he received for purposes of establishing his maximum liability under § 6324(b) because the issue was not actually litigated in the tax court proceeding. App. 46a; R.1033-34. The district court subsequently struck the opinion of the Government's valuation expert, who had not been made aware of the dispute as to Birnie's title to the Hondo stock that existed at the time of the 1980 transfers and conceded that the existence of this dispute rendered any valuation of the stock interest Birnie transferred to Mr. Davenport "speculative and subjective." R.1209, 1590. The dis-

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[5] In its summary judgment briefing, the Government repeatedly argued that res judicata barred only relitigation of the tax liability of Birnie's estate and that *collateral estoppel alone* barred litigation of the value of the stock:

> *Collateral estoppel* binds Davenport to [the] determined *stock value* . . . .
> Davenport is bound to the Tax Court's determination of *gift tax* due through res judicata (claim preclusion). As to the determination of *individual issues* that formed the building blocks of the Tax Court's gift tax determination, . . . *collateral estoppel (issue preclusion) applies.* . . .
> *Res judicata* bars [a] global attack to challenge the *amount of tax due. Collateral estoppel* bars relitigation of specific building block issues . . . .
> With respect to the *stock itself*, Davenport is bound to the value determined by the Tax Court *through collateral estoppel.*

R. 946, 956, 957, 959-60 (emphases added).

trict court thereafter granted summary judgment for Mr. Davenport because the Government had no evidence of the value of the property he received from Birnie in 1980, and thus no evidence to support imposition of any amount of personal liability under § 6324(b). R.1728.

The Government appealed to the Fifth Circuit, arguing for the first time that res judicata—as opposed to collateral estoppel—precluded Mr. Davenport from contesting the value of the inchoate stock interest he received from Birnie.[6] The Fifth Circuit reversed the judgment of the district court based on this new argument, holding that "res judicata binds Gordon Davenport to the value of the Hondo stock established in the tax proceeding." App. 17a. Thus, the Fifth Circuit held that Mr. Davenport owes the Government over $640,000[7] on account of a gift the Government claims he received nearly thirty years ago, even though neither Mr. Davenport nor anyone else has ever actually litigated the issues of whether

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[6] The Government raised this contention in passing in its objections to the magistrate judge's report and recommendation, R.1037; however, it never presented the issue in summary judgment briefing before the magistrate judge. The Government first fully briefed its contention that res judicata precludes Mr. Davenport from litigating the value of the stock interest on appeal—only *after* the district court struck its valuation expert and held that the Government lacked any evidence to carry its burden of proving the value of the stock interest.

[7] This figure represents the value of the imputed gift to Mr. Davenport, assuming a stock value of $2000 per share.

he even received a gift,[8] and, if so, the value of the gift at the time he received it.

REASONS FOR GRANTING THE PETITION

The Fifth Circuit's holding that the tax court's adjudication of Birnie's tax liability precludes Mr. Davenport from litigating his status as a transferee and the value of the stock interest Birnie transferred to him creates a circuit split that this Court should resolve. The Fifth Circuit's holding conflicts with the decisions of all other circuits to have considered the issue. For seventy years those courts have uniformly held that, while a prior tax liability adjudication against a transferor precludes a § 6324 defendant from litigating the transferor's tax liability, it does *not* preclude the alleged transferee from litigating other elements of the § 6324 claim, including transferee status and the value of the property transferred. Indeed, that is precisely what the Tenth Circuit held on these same facts.

The Fifth Circuit's application of res judicata also eviscerates the Tax Code's allocation of the burden of proof to the Government in transferee liability proceedings. Specifically, it allows the Government to rely on factual findings from a tax court proceed-

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[8] While the tax court determined that an inchoate interest in stock was transferred to Mr. Davenport in 1980, whether that transfer constituted a gift depends upon whether the fair market value of the stock interest exceeded the $804 per share purchase price he agreed to pay at the time. Given that the value of the stock has never been litigated, whether the conveyance constituted a gift has never been litigated either.

ing in which the Government *does not* bear the burden of proof to establish factual issues in a subsequent transferee liability proceeding in which the Government *does* bear the burden of proof.

Absent review by this Court, determinations of a transferor's tax liability will have a far broader preclusive effect in subsequent transferee liability proceedings that the Government initiates in the Fifth Circuit than the same determinations would have in transferee liability proceedings initiated in any other circuit. Such a result is neither fair to litigants nor consistent with the constitutional and congressional mandate of uniform construction and application of the Tax Code.

I. THE FIFTH CIRCUIT'S USE OF RES JUDICATA TO ESTABLISH TRANSFEREE LIABILITY UNDER THE TAX CODE CONFLICTS WITH DECISIONS OF OTHER FEDERAL COURTS, INCLUDING THE TENTH CIRCUIT'S HOLDING ON IDENTICAL FACTS.

The Fifth Circuit held that the res judicata effect of the tax court's adjudication of Birnie's gift tax liability "binds [Mr.] Davenport to the value of the Hondo stock established in the tax proceeding," even though the valuation resulted from a stipulation rather than actual litigation. App. 17a. The Fifth Circuit acknowledged that its holding is in direct conflict with the Tenth Circuit's holding—on these very same facts—that principles of collateral estoppel rather than res judicata determine whether a

§ 6324 defendant is precluded from litigating particular factual issues that may also have been germane to the tax liability claim against the transferor, such as transferee status and value of the property transferred. *See Botefuhr*, 309 F.3d at 1281-83. The Tenth Circuit held that, because the value of the stock interest transferred to Birnie's niece and nephews was not actually litigated in the tax court proceeding, collateral estoppel did not preclude Vestal from litigating this issue for purposes of determining the scope of her § 6324(b) liability. *See id.* at 1283.[9] Had the Fifth Circuit applied the Tenth Circuit's analysis, it would have concluded that Mr. Davenport, like Vestal, is not precluded from litigating the value of the stock interest Birnie transferred to him.

The basis of the Fifth Circuit's holding—and the core of its conflict with the Tenth Circuit—is its conclusion that a § 6324 transferee liability claim constitutes the same claim as the tax liability claim against the transferor. App. 12a-13a. Thus, in the Fifth Circuit, the res judicata effect of a prior adjudication of the tax liability claim precludes litigation of

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[9] Law of the case binds the Government to this conclusion that collateral estoppel does not apply because the issue was conclusively adjudicated against the Government before the case against Mr. Davenport was transferred for want of jurisdiction. *See United States v. 49.01 Acres of Land*, 802 F.2d 387, 389-90 (10th Cir. 1986); *see also Int'l Union, UAW v. Donovan*, 756 F.2d 162, 165 (D.C. Cir. 1985) ("[W]e will adopt and give full effect to otherwise valid orders entered by the lower court prior to transfer [of the case for lack of jurisdiction] . . . . We will treat these orders essentially as being the law of the case . . . .").

factual issues pertinent to the transferee liability claim. As demonstrated below, the Fifth Circuit's same-claim holding conflicts not only with the holding of the Tenth Circuit, but also with the holdings of every other court to have addressed the issue.

This Court has long observed that res judicata (claim preclusion) and collateral estoppel (issue preclusion) are related but distinct preclusion doctrines. As its alternative name suggests, res judicata prevents relitigation of *claims*—i.e., it "puts an end to the cause of action, which cannot again be brought into litigation between the parties upon any ground whatever," regardless of whether the ground or issue was actually litigated when the claim was first adjudicated. *Nevada v. United States*, 463 U.S. 110, 129-30 (1983).

By contrast, collateral estoppel precludes relitigation of particular *issues*. Collateral estoppel operates to preclude litigation of a particular issue in a second suit even if the claim or cause of action involved in the second suit is different from a previously adjudicated claim involving the same issue, but *only if* the issue was *actually litigated* in connection with the prior claim. *See Parklane Hosiery Co., Inc. v. Shore*, 439 U.S. 322, 326 (1979) ("Under the doctrine of collateral estoppel, on the other hand, the second action is upon a different cause of action and the judgment in the prior suit precludes relitigation of issues actually litigated and necessary to the outcome of the first action."). Thus, while res judicata and collateral estoppel both involve successive litigation entailing overlapping issues or elements, the distinction between the application of res judicata

and collateral estoppel hinges upon whether the claim adjudicated in a prior action constitutes the same claim asserted in a subsequent action.

A § 6324 transferee liability claim has the following elements: (1) tax liability on the part of a transferor; (2) the transferor's failure to pay the tax when due; (3) transfer of property by the transferor to the § 6324 defendant (transferee status); and (4) value of the property transferred to the transferee (which establishes the upper limit of the defendant's transferee liability). *See* 26 U.S.C. § 6324(b). The Government bears the burden of proving each of these elements other than the transferor's tax liability. *See Sather v. Comm'r*, 251 F.3d 1168, 1176 (8th Cir. 2001) ("The IRS must prove only that the transferee was the recipient of a taxable transfer, the gift tax was not paid when due, and the extent of the value of the gift.").

If, as the Fifth Circuit has concluded, the § 6324 transferee liability claim were the same claim as the tax liability claim against the transferor, such that res judicata rather than collateral estoppel determines the preclusive effect of the adjudication of one claim on the other, then the § 6324 defendant would be foreclosed from litigating *any element* of the § 6324 claim because res judicata prevents supporting or defending the claim on "*any ground whatever*," including the ground that particular elements of the claim are unproven. *Nevada*, 463 U.S. at 129-30 (emphasis added).[10] Yet, *for seventy years*, federal

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[10] While the Fifth Circuit couched its holding in terms of precluding Mr. Davenport's litigation of a particular factual

courts have uniformly held that, notwithstanding a prior tax liability adjudication against a transferor, the transferee may litigate all elements of the transferee liability claim other than the transferor's tax liability.

In *First National Bank v. Commissioner*, 112 F.2d 260 (7th Cir. 1940), the court held that, because a transferor and transferee are deemed to be in privity with respect to the existence and amount of the transferor's tax liability, "a judgment against a transferor for taxes . . . may, consistently with due process of law, be treated as concluding the transferee respecting the existence and amount of indebtedness so adjudged." *Id.* at 262. However, the court went on to hold that the transferee "is entitled upon the most fundamental principles to his day in court and a hearing . . . to show that he has not received property as transferee sufficient to discharge the liability." *Id.*; *see also Pert v. Comm'r*, 105 T.C. 370, 371 (1995) (holding that the preclusive effect of a tax liability adjudication against a transferor prevented an alleged transferee from relitigating the transferor's tax liability, but "leav[ing] certain other issues for trial, such as whether (or to what extent) petitioner is a transferee."). In other words, a prior tax court adjudication precludes the alleged transferee from relitigating the transferor's indebtedness, but it

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element pertinent to the § 6324 claim—specifically, "the value of the Hondo stock established in the tax court proceeding" (App. 17a)—the effect of the Court's holding is that Mr. Davenport is precluded from litigating the § 6324 claim *at all* because the *claim*—as opposed to some discrete *element* of the claim—has already been adjudicated against him.

does not preclude the alleged transferee from litigating either his transferee status or the value of the property transferred.

The Eleventh Circuit's decision in *Baptiste v. Commissioner*, 29 F.3d 1533 (11th Cir. 1994), on which the Fifth Circuit relied as the primary support for its holding, also makes clear that a prior adjudication of the transferor's tax liability does not preclude a § 6324 defendant from litigating elements of the transferee liability claim other than the transferor's tax liability.[11] Specifically, the Eleventh Circuit held that Baptiste was a transferee, *not* based on the res judicata effect of the tax court determination of the transferor's tax liability, but rather based on a determination that the facts alleged in the Government's pleadings, which were deemed admitted under a tax court procedural rule by virtue of Baptiste's failure to deny them, "are sufficient to establish, as a matter of law, Baptiste's status as a transferee." *Baptiste*, 29 F.3d at 1538. This determination would have been superfluous if the prior tax court decision's res judicata effect precluded Baptiste

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[11] The Fifth Circuit also relied upon *Baptiste v. Commissioner*, 29 F.3d 433 (8th Cir. 1994), which addressed a claim of alleged transferee liability involving the same transferor at issue in the Eleventh Circuit's decision cited above. The alleged transferee in the Eighth Circuit case challenged neither his transferee status nor the value of the property transferred to him. The Eighth Circuit therefore had no occasion to address whether the res judicata effect of the adjudication of the transferor's tax liability would preclude the alleged transferee from challenging his transferee status or the value of property transferred to him.

from contesting his transferee status as well as the transferor's tax liability.[12]

These holdings that § 6324 defendants are permitted to litigate elements of the transferee liability claim other than the transferor's tax liability demonstrate that the courts have uniformly concluded that a transferee liability claim cannot constitute the same claim as an underlying tax liability claim against the transferor for purposes of res judicata; otherwise, res judicata would preclude litigation of *any element* of the transferee liability claim. The Fifth Circuit's holding thus creates a circuit split.

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[12] Certain cases addressing the preclusive effect of a prior tax court adjudication of transferor tax liability upon a subsequent transferee liability proceeding identify res judicata rather than collateral estoppel as the preclusion doctrine that prevents the alleged transferee from litigating the transferor's tax liability. *See, e.g., Pert*, 105 T.C. at 376-77; *Baptiste*, 29 F.3d at 1540. The reason for this characterization is that, while the transferor's tax liability is an independent *claim* against the transferor, it is merely a single *element* of the § 6324 claim against the transferee. App. 11a ("Generally, '[t]he tax liability of a particular tax for a particular taxable year' is a *single cause of action*." (citing 15 Elizabeth K. Berman, Mertens Law of Federal Income Taxation § 60:33 (2000) (emphasis added)).

It does not follow from this characterization, however, that the entire § 6324 claim, which merely includes the transferor's tax liability as one of its *elements*, constitutes the *same claim* as the transferor tax liability claim, such that res judicata *also* precludes the alleged transferee from litigating elements of the § 6324 claim *other than the transferor's tax liability*, as the Fifth Circuit incorrectly concluded.

II. THE FIFTH CIRCUIT'S HOLDING CONTRAVENES FUNDAMENTAL PRINCIPLES OF CLAIM AND ISSUE PRECLUSION ARTICULATED BY THIS COURT.

The Fifth Circuit's holding that the § 6324 transferee liability claim against Mr. Davenport constitutes the same claim as the tax liability claim previously adjudicated against Birnie's estate is inconsistent with fundamental principles of claim and issue preclusion articulated by this Court. This Court has held that a subsequently-asserted claim is the same as a prior claim, such that res judicata rather than collateral estoppel operates to determine the preclusive effect of the prior adjudication, only when the subsequently-asserted claim was or *could have been* asserted in the prior action. *See Brown v. Felsen*, 442 U.S. 127, 131 (1979) ("Res judicata prevents litigation of all grounds for, or defenses to, recovery that were *previously available to the parties*, regardless of whether they were asserted or determined in the prior proceeding." (emphasis added)); *Eubanks v. F.D.I.C.*, 977 F.2d 166, 174 (5th Cir. 1992) ("The critical question for res judicata purposes is whether the party could or should have asserted the claim in the earlier proceeding.").

The § 6324 transferee liability claim against Mr. Davenport was not and could not have been asserted in the tax court proceeding regarding Birnie's estate and therefore cannot be the same claim as the tax liability claim. Mr. Davenport was not even a party to the tax court proceeding initiated by Birnie's estate. Indeed, he *could not have been* a party because Mr. Davenport had not been issued a

notice of deficiency or liability;[13] accordingly, the tax court would have lacked jurisdiction over any attempted intervention by Mr. Davenport. *See Siegel's Estate v. Comm'r*, 67 T.C. 1033, 1038 (1977) ("The record shows that no notice of deficiency or of liability as transferee has been issued to any of the persons seeking to intervene in this case. . . . Since no notice of deficiency has been issued to any of the moving parties, it is clear . . . that they may not be joined as parties in this case."); *Guarino v. Comm'r*, 67 T.C. 329, 331 (1976). This forecloses a conclusion that the tax liability claim at issue in the tax court proceeding is the same as the transferee liability claim at issue here.

It is true, as the Fifth Circuit observed, that a transferor is deemed to be in privity with the transferee with regard to the final adjudication of the transferor's tax liability. App. 11a. However, the presence of privity cannot render the transferee liability claim against the alleged transferee the same claim or cause of action as the tax liability claim adjudicated against the transferor in an action to which the alleged transferee was not a party. This

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[13] While the IRS has the option of assessing transferee liability by sending a notice of liability to the alleged transferee, *see* 26 U.S.C. § 6901, such an assessment is not a prerequisite to a suit under § 6324. *See United States v. Geniviva*, 16 F.3d 522, 524 (3rd Cir. 1994) (citing *Leighton v. United States*, 289 U.S. 506, 507-08 (1933)); *United States v. Russell*, 461 F.2d 605, 606 (10th Cir. 1972); *Ripley v. Comm'r*, 102 T.C. 654, 659 (1994) ("[R]espondent was not required to issue a notice of transferee liability to petitioner pursuant to section 6901(a) or otherwise assess petitioner prior to taking steps . . . to enforce the special gift tax lien arising under section 6324(b)").

Court has long acknowledged that any preclusive effect of a judgment in a prior action upon a subsequent action by or against one who is in privity with a party to the prior action, but who was not himself a party to that action, necessarily "falls under the rubric of collateral estoppel rather than res judicata because the latter doctrine presupposes identity between causes of action. And the cause of action [asserted in the prior action, even though arising from the same transaction as the subsequent action,] *differs by definition* from that which [the privy] subsequently seeks to litigate in his own right." *Montana v. United States*, 440 U.S. 147, 154 (1979) (emphasis added); *see also* Note, Developments in the Law—Res Judicata, 65 Harv. L. Rev. 818, 862 (1952) ("Any such [preclusive] effect [of a prior judgment on a non-party to the action in which the judgment was entered] must arise through operation of collateral estoppel; *since a different party is involved in the second action, the 'cause of action' must be different.*" (emphasis added)); Restatement (Second) Judgments § 39 (1982), comment b (noting that, even where a non-party controls prior litigation to a sufficient extent that the judgment entered in the action may be given preclusive effect in a subsequent action by or against the non-party, only issue preclusion rather than claim preclusion applies in the subsequent action "because the person controlling the [first] litigation, as a nonparty, is by definition asserting or defending a claim other than one he himself may have").

It is thus apparent that the § 6324(b) claim at issue here, which was not and could not have been

asserted in the tax court proceeding, cannot constitute the same claim as the tax liability claim against Birnie's estate for res judicata purposes.[14] The Court should grant certiorari to correct the Fifth Circuit's contrary holding, thereby addressing the circuit split the Fifth Circuit's holding creates and ensuring appropriate application of this Court's precedent. Given the extent of the Fifth Circuit's departure from well-established principles of claim and issue preclusion, summary reversal may even be warranted.

III. THE FIFTH CIRCUIT'S HOLDING EVISCERATES THE TAX CODE'S ALLOCATION OF THE BURDEN OF PROOF IN TRANSFEREE LIABILITY SUITS.

"In a transferee liability case, . . . [the Government] must prove all of the elements of transferee liability except that [it] does not have the burden of proving that the transferor was liable for the tax." *Locke v. Comm'r*, 72 T.C.M. (CCH) 1481 (1996); *see also* 26 U.S.C. § 6902(a) ("[T]he burden of proof shall be upon the Secretary to show that a petitioner is liable as a transferee of property of a taxpayer, but not to show that the taxpayer was liable for the

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[14] As a chronological matter, a transferee liability claim does not even accrue until after the tax liability claim against the transferor because one element of the transferee liability claim is proof that the tax was "not paid when due." 26 U.S.C. § 6324(b). Congress's enactment of different statutes of limitation applicable to transferor tax liability and subsequent transferee liability claims constitutes another telling indication that the claims cannot be the same for purposes of res judicata. *Compare* 26 U.S.C. § 6501 *with id.* § 6901.

tax."). By contrast, in a tax liability proceeding, *the taxpayer* bears the burden of proving that the Government's determination of tax liability is erroneous. *See* Tax Rule 142(a); *Healy v. Comm'r*, 345 U.S. 278, 283 n.15 (1953) (noting that the burden of proof in a transferee liability proceeding "may be contrasted to the rule that normally the burden of proof is on the taxpayer contesting the determination of the Commissioner").

Thus, as the tax court observed, Birnie's estate bore the burden of proving that the gift tax delinquency assessed by the Government was incorrect—i.e., of proving either (1) that no gift to Mr. Davenport or his cousins that would give rise to gift tax liability occurred in 1980 or (2) that the valuation of the stock interest the Government used to calculate the value of the alleged gift and the amount of associated gift tax was incorrect. App. 78a ("The burden of proof lies with petitioner."). In this § 6324 suit against Mr. Davenport, however, the burden of proving that Mr. Davenport received a gift from Birnie in 1980 and, if so, the value of the gift received is upon the Government.

Allowing the Government to invoke res judicata to preclude Mr. Davenport from litigating his transferee status or the value of property he received eviscerates the Tax Code's allocation of the burden of proof to the Government on these issues. If factual findings from a tax liability proceeding in which the Government *does not* bear the burden of proof are given preclusive effect in a transferee liability proceeding in which the Government *does* bear the burden of proof, then the allocation of the burden of

proof to the Government in the transferee liability proceeding is meaningless because preclusion effectively transfers the burden back to the alleged transferee.[15] Accordingly, res judicata cannot apply.[16] *See* Restatement (Second) Judgments § 28 (1982) ("Although an issue is actually litigated and determined by a valid and final judgment, and the determination is essential to the judgment, relitigation of the issue in a subsequent action between the parties is not precluded [where] . . . *the burden [of proof] has shifted to [the other party* in the subsequent action] . . . ." (emphasis added)); *cf. Helvering v. Mitchell*, 303 U.S. 391, 397 (1938) ("The difference in degree of the

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[15] By contrast, giving preclusive effect *only* to the determination of the tax liability of the transferor—as all the cases to address the issue prior to the Fifth Circuit have done, *see* Section 1, *supra*—is wholly consistent with the allocation of the burden of proof contemplated by the Tax Code, which specifically provides that the Government does *not* bear the burden of proving the transferor's tax liability but *does* bear the burden on all other elements of transferee liability. 26 U.S.C. § 6902(a).

[16] Applying res judicata to relieve the Government of its obligation to carry the burden of proof on the value of the property transferred to Mr. Davenport is particularly pernicious, given that the Government's own valuation expert concedes that the Government *could not carry that burden* because the dispute as to Birnie's title to the stock at the time of the transfer renders any opinion regarding the value of the interest she transferred at that time inherently speculative, unreliable, and thus inadmissible. *See* Fed. R. Evid. 702; *Daubert v. Merrell Dow Pharmaceuticals, Inc.*, 509 U.S. 579 (1993).

burden of proof in criminal and civil cases precludes application of the doctrine of res judicata.").[17]

IV. RESOLUTION OF THE CIRCUIT SPLIT CREATED BY THE FIFTH CIRCUIT'S RULING IS CRITICAL TO MAINTAINING CONSTITUTIONALLY AND CONGRESSIONALLY MANDATED UNIFORMITY IN CONSTRUCTION AND APPLICATION OF THE TAX CODE.

"It can hardly be denied that uniformity in the imposition and collection of federal taxes has always been regarded as extremely desirable in this country." *Comm'r v. Stern*, 357 U.S. 39, 48-49 (1958) (Black, J., dissenting). Indeed, uniform application of the tax laws is constitutionally mandated: "all Duties, Imposts and Excises [levied by Congress] shall be uniform throughout the United States." U.S. Const. art. 1, § 8, cl. 1. "Taxpayers should be treated equally without regard to the fortuity of residence . . . ." *Stern*, 357 U.S. at 49. This Court has long held that the constitutionally mandated

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[17] Certainly, if Congress believed that tax liability and transferee liability claims were one and the same, it would have had no occasion to enact a statute establishing a different burden of proof for transferee liability claims. This Court has long recognized that judicial decisions should not render statutory language meaningless or thwart Congressional intent as expressed in the statutory language; yet this is the precise effect of the Fifth Circuit's holding. *See Beck v. Prupis*, 529 U.S. 494, 506 (2000) (noting the "longstanding canon of statutory construction that terms in a statute should not be construed so as to render any provision of that statute meaningless or superfluous").

uniformity of taxation occurs only when a tax "operates with the same force and effect in every place where the subject of it is found." *Edye v. Robertson*, 112 U.S. 580, 594 (1884); *see also Burnet v. Harmel*, 287 U.S. 103, 110 (1932) (holding that the Tax Code "is to be interpreted so as to give a uniform application to a nation-wide scheme of taxation").

The Fifth Circuit's holding that the res judicata effect of a prior tax court determination precludes an alleged transferee from litigating his transferee status or the value of property transferred to him by the party primarily liable for the tax undermines the constitutional and congressional mandate of uniform construction and application of the Tax Code. The Fifth Circuit's holding directly conflicts with seventy years of precedent from other courts to have considered the claim-preclusive effect of a prior tax liability determination upon a § 6324 defendant's entitlement to litigate discrete factual elements of the § 6324 transferee liability claim other than the transferor's tax liability. As noted above, all of the cases to have addressed the issue before the Fifth Circuit have held, either explicitly or implicitly, that the preclusive effect of a tax liability adjudication precludes an alleged transferee from litigating *only* the transferor's tax liability; it does *not* preclude the alleged transferee from litigating his transferee status or the value of the property purportedly transferred to him. Further, the Fifth Circuit's departure from this line of precedent violates fundamental principles of claim and issue preclusion articulated by this Court and renders the Tax Code's express allocation of the burden of proof

to the Government in transferee liability cases meaningless.

Absent review by this Court, a stipulation in a tax court proceeding regarding a fact pertinent to tax liability will have much broader preclusive effect in § 6324 transferee liability proceedings the Government initiates in the Fifth Circuit than the *exact same* stipulation would have in transferee liability proceedings initiated in other circuits. In the Fifth Circuit, the transferor's stipulation to unlitigated factual issues will bind the transferee and relieve the Government of its statutory burden of proving the stipulated issues in the transferee liability case; in every other circuit, it will not. The inconsistency and uncertainty created by the Fifth Circuit's erroneous holding is neither fair to the litigants in such actions nor consistent with the congressional and constitutional mandate of uniform, consistent application of the Tax Code.

Review by this Court is necessary to correct the Fifth Circuit's serious legal error and ensure that alleged § 6324 transferees in all jurisdictions are treated consistently and in accordance with the statutory scheme mandated by the Constitution and the Congress.

CONCLUSION

For the foregoing reasons, the petition for a writ of certiorari should be granted.

Respectfully submitted,

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August 2007

APPENDIX

APPENDIX A

United States Court of Appeals
FILED
April 9, 2007
Charles R. Fulbruge, III, Clerk

IN THE UNITED STATES COURT OF APPEALS
FOR THE FIFTH CIRCUIT

No. 06-40466

UNITED STATES OF AMERICA
Plaintiff - Appellant
v.
BIRNIE DAVENPORT, ET AL
Defendants
GORDON E DAVENPORT
Defendant – Appellee

Appeal from the United States District Court
for the Southern District of Texas, Galveston

Before KING, GARZA, and PRADO, Circuit Judges.

KING, Circuit Judge:

In an action to determine the federal tax liability of the estate of Birnie Davenport, the tax court held that the estate was liable for the unpaid gift tax on inter-vivos gifts of stock made by Birnie Davenport to her two nephews, Gordon Davenport and Charles Botefuhr, and her niece, Patricia Vestal.

Because the estate did not pay the tax, the government now seeks to collect it from Gordon Davenport under the provisions of the Internal Revenue Code imposing liability for an unpaid gift tax on the transferee of the gift. The district court held that Gordon Davenport was not bound by the doctrine of res judicata to certain key determinations made by the tax court. Because we agree with the government that this case involves the same nucleus of operative facts as the proceeding in the tax court, and that as a result res judicata applies, the district court's judgment is REVERSED.

I. FACTUAL AND PROCEDURAL BACKGROUND

Birnie and Elizabeth Davenport, who were sisters, lived together much of their adult lives. Over many years, the two sisters commingled all of their earnings and assets. Pursuant to a long-standing oral agreement between the two, Elizabeth Davenport held legal title to the assets, but the sisters shared equally in the profits and losses of their investments. They considered all of their assets to be jointly owned, and their income tax returns filed over many years reflected this belief. Each of the sisters filed a separate income tax return in which she reported her earnings from her job and an equal share of profits and losses from the joint investments. The IRS accepted this split of investment income and expenses throughout numerous audits between 1965 and 1979.

The sisters' investments included stock in Hondo Drilling Company. At the time of Elizabeth

Davenport's death in 1979, the sisters owned 3220 shares of Hondo stock. The sisters had two nephews, Gordon Davenport and Charles Botefuhr, and one niece, Patricia Vestal. Gordon Davenport, Botefuhr, and Vestal were appointed co-executors of Elizabeth Davenport's estate.[1] In July 1980, slightly more than six months after her sister's death, using two conveyance methods, Birnie Davenport transferred half (1610 shares) of the Hondo stock to her niece and nephews. First, she transferred 537 shares to Gordon Davenport and 536 shares to Vestal through installment sale agreements, with the stock being valued in the agreements at $804 per share.[2] Birnie Davenport reported the installment sales on her 1980 income tax return and indicated on that form that the sales were to related parties.[3] Second, Birnie Davenport transferred 537 shares to Botefuhr as an outright gift. In a signed "Family Agreement," Botefuhr promised to file the appropriate gift tax return that would report the gift made by Birnie Davenport and to pay on her behalf the gift taxes associated with his gift. Botefuhr did not fulfill this responsibility. In July 1981, Hondo Drilling

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[1] Botefuhr resigned his position after a dispute concerning how to report assets held in Elizabeth Davenport's name.

[2] This transaction also included seventy-five shares of Union Supply Company stock. Because the Hondo stock accounted for most of the transaction's value, we will refer only to the Hondo stock.

[3] In 1982, Birnie Davenport forgave the remaining balance on Gordon Davenport's and Vestal's promissory notes. Birnie Davenport's 1983 gift tax return reported forgiving the promissory notes and reported and paid $71,911 in gift tax liability.

Company redeemed Botefuhr's shares at $2190 per share.[4]

Birnie Davenport died in 1991. Gordon Davenport, Vestal, and Botefuhr were appointed as personal representatives of her estate. While preparing Birnie Davenport's estate tax return in 1991, Corrine Childs, the Davenport sisters' long-time tax attorney, learned that Botefuhr had not filed the 1980 gift tax return or paid the taxes as promised. When Vestal and Gordon Davenport filed the estate tax return, they filed a gift tax return reporting the 1980 gift to Botefuhr at $804 per share. The estate paid a gift tax of $95,322 with the return. Botefuhr did not sign either the gift tax return or the estate tax return.

In 1992 the IRS initiated an audit of Birnie Davenport's estate tax return and 1980 gift tax return and ultimately determined that Birnie Davenport's gift of Hondo stock to Botefuhr should have been valued at $2730 per share rather than $804 per share. The large discrepancy in values created a correspondingly large gift tax deficiency,

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[4] During this time, the IRS investigated the estate tax owed by Elizabeth Davenport. The investigation culminated late in 1982. The report concluded that: (1) all of the property held in Elizabeth Davenport's name, including all of the Hondo stock, should be included in her estate and (2) that Birnie Davenport's prior conveyances were ineffective. The estate settled the claim at a valuation of $2,400 per share of Hondo stock so that the IRS would abandon its claim that all of the property recorded in Elizabeth Davenport's name belonged only to her. Thus, the settlement cleared up title concerns on Birnie Davenport's half of the property.

which Birnie Davenport's estate contested in tax court. *See Estate of Davenport v. Comm'r*, 74 T.C.M. (CCH) 405 (1997). One issue before the tax court was whether Birnie Davenport made a completed gift to Gordon Davenport, Vestal, and Botefuhr. *Id.* at 411. The tax court held that even though Birnie Davenport did not have legal title at the time of the transfers, she did effect inter vivos gifts to Gordon Davenport, Vestal, and Botefuhr of the Hondo stock, which the tax court valued at $2000 per share.[5] *Id.* at 407, 412. A second issue before the tax court was whether the statute of limitations barred the government from recovering the gift tax due. The tax court held that the statute of limitations did not bar assessment of gift tax liability because with respect to each of the transfers, the limitations period started running on November 7, 1991, when Vestal and Gordon Davenport filed Birnie Davenport's 1980 gift tax return. *Id.* at 412. In accordance with its findings, the court calculated the tax deficiency owed by the estate.[6] The Tenth Circuit affirmed the tax

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[5] The tax court decided this value and incorporated by reference the parties' stipulation of fact which read:

> 38. For the purposes of this litigation, if the Court finds that Birnie Davenport transferred Hondo stock to Patricia Vestal, Gordon Davenport, and Charles Botefuhr in the calendar quarter ending September 30, 1980, the parties agree that the fair market value of such Hondo stock was $2,000.00 per share at the time of the transfers.

[6] The tax court determined that the estate's deficiency in unpaid gift taxes was $822,653, that the estate owed an additional penalty of $205,663 for the failure to timely file the

court's decision. *Estate of Davenport v. Comm'r*, 184 F.3d 1176, 1188 (10th Cir. 1999) (holding that Birnie Davenport "had a sufficient ownership interest in the Hondo stock . . . to effect inter vivos transfers of [it]" and that Birnie Davenport completed gifts during July 1980 to her two nephews and niece).

Despite the tax court's decision, the estate did not pay the taxes owed. Because the tax court lacks the authority to enforce its judgments, the government filed the current action in the Northern District of Oklahoma against the estate and all three cousins to reduce to judgment the estate's liability and the donees' liability as transferees pursuant to I.R.C. § 6324(b). *See United States v. Estate of Davenport*, 159 F. Supp. 2d 1330, 1332 (N.D. Okla. 2001). The estate conceded liability. *Id.* The government also sought individual liability against the three cousins in their capacity as co-executors pursuant to 31 U.S.C. § 3713 for allegedly making improper distributions from the estate before paying the federal tax liabilities. *Id.* The district court dismissed the § 3713 claim pre-trial. *Id.*

Although Gordon Davenport and Botefuhr contested jurisdiction, the district court overruled their motions to dismiss for lack of personal jurisdiction. *Id.* at 1335. On appeal, the Tenth Circuit held that the Oklahoma district court did not have jurisdiction over Botefuhr and Gordon

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1980 gift tax return, and that the estate owed interest on both the unpaid gift taxes and the penalty. In 1998 the IRS assessed that with penalties and interest, the estate's tax bill amounted to about $5.2 million.

Davenport after dismissing the § 3713 claim. *United States v. Botefuhr*, 309 F.3d 1263, 1274 (10th Cir. 2002).

The case was remanded to the Oklahoma district court, which transferred Botefuhr's case to the Western District of Texas and Gordon Davenport's case to the Southern District of Texas. The case before this panel involves solely Gordon Davenport's appeal.

The Southern District of Texas ruled on multiple motions for summary judgment by Gordon Davenport and the government. First it determined that the statute of limitations barred assessment of the gift tax on the imputed gift arising from the July 1980 installment sale, but that the statute of limitations did not bar assessment of the gift to Botefuhr. Second, it held that although res judicata and collateral estoppel bound Gordon Davenport to the tax court's finding that he was a donee, neither doctrine established the value of the gift to him (the Hondo stock) or the amount of his liability. Finally, the district court held that the government failed to provide any evidence on damages, an essential element of its claim, and it granted summary judgment against the government. The government now appeals.

II. DISCUSSION

The Internal Revenue Code imposes tax liability "on the transfer of property by gift." I.R.C. § 2501(a). The definition of a gift includes transfers of property for "less than an adequate and full

consideration in money or money's worth." I.R.C. § 2512. The donor, as the party who makes the gift, bears the primary responsibility for paying the gift tax. See I.R.C. § 2502 (c) ("The tax imposed by 2501 shall be paid by the donor."). When, as here, the donor dies before paying the gift tax owed, the personal representative of the estate is responsible for paying the tax out of the estate, as a debt against the donor's estate. Treas. Reg. § 25.2502-2. The donee may also be held personally liable for the full amount of any unpaid gift tax pursuant to 26 U.S.C. § 6324(b).[7] Although the donee's liability is limited to the value of the gift he received from the donor, he may be forced to pay more than the gift tax attributable to his gift. § 6324 (b); see also 14 EDWARD J. SMITH, MERTENS LAW OF FEDERAL INCOME TAXATION § 53: 42 (2004). Thus, Gordon Davenport is liable for all the gift tax owed by the estate for 1980, up to the value of the gift he received.

The government seeks to collect unpaid gift taxes owed by the Birnie Davenport estate from Gordon Davenport pursuant to the transferee liability provision of I.R.C. § 6324(b). The government argues that the tax court's decision is res judicata as to the liability of Gordon Davenport, and that accordingly, Gordon Davenport may not relitigate the value of the Hondo stock or whether the statute of limitations expired on the gifts to Gordon Davenport, Vestal, and Botefuhr.

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[7] Section 6324(b) states: "If the tax is not paid when due, the donee of any gift shall be personally liable for such tax to the extent of the value of such gift." I.R.C. § 6324(b).

The term "res judicata" is often used to describe two discrete preclusive doctrines: res judicata and collateral estoppel.[8] *Baker v. Gen. Motors Corp.*, 522 U.S. 222, 233 n.5 (1998). These doctrines "relieve parties of the cost and vexation of multiple lawsuits, conserve judicial resources, and, by preventing inconsistent decisions, encourage reliance on adjudication." *Allen v. McCurry*, 449 U.S. 90, 94 (1980). Under the doctrine of res judicata, "a final judgment on the merits bars further claims by parties or their privies based on the same cause of action." *Montana v. United States*, 440 U.S. 147, 153 (1979). The bar prevents relitigation of all "issues that were or could have been raised in [the previous] action." *Federated Dep't Stores, Inc. v. Moitie*, 452 U.S. 394, 398 (1981). In contrast, under the doctrine of collateral estoppel, "the second action is upon a different cause of action and the judgment in the prior suit precludes relitigation of issues actually litigated and necessary to the outcome of the first action." *Parklane Hosiery Co. v. Shore*, 439 U.S. 322, 327 n.5 (1979).

This court reviews the res judicata effect of a prior judgment de novo because it is a question of law.[9] *Test Masters Educ. Servs., Inc. v. Singh*, 428

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[8] Res judicata is also known as claim preclusion, and collateral estoppel as issue preclusion.

[9] Gordon Davenport contends that the government acknowledged before the district court that res judicata applies only to the estate's liability, and not his donee liability or the valuation of the stock. A review of the government's response to Gordon Davenport's second motion for summary judgment and its cross-motion for partial summary judgment regarding valuation indicates that the government argued, inter alia, that

F.3d 559, 571 (5th Cir. 2005). For res judicata to apply, the following four-part test must be satisfied: (1) the parties must be either "identical or in privity; (2) the judgment in the prior action [must have been] rendered by a court of competent jurisdiction; (3) the prior action must have been concluded to a final judgment on the merits; and (4) the same claim or cause of action [must have been] involved in both actions." *In re Southmark Corp.*, 163 F.3d 925, 934 (5th Cir. 1999); *see also* 15 ELIZABETH K. BERMAN, MERTENS LAW OF FEDERAL INCOME TAXATION § 60: 32 (2000).

This court determines whether two suits involve the same claim or cause of action by applying the transactional test of the Restatement (Second) of Judgments, § 24. *Petro-Hunt, L.L.C. v. United States*, 365 F.3d 385, 395 (5th Cir. 2004). Under the transactional test, our inquiry focuses on whether the two cases under consideration are based on "the same nucleus of operative facts." *In re Southmark Corp.*, 163 F.3d at 934 (quoting *In re Baudoin*, 981 F.2d 736, 743 (5th Cir. 1993)). The nucleus of operative facts, rather than the type of relief requested, substantive theories advanced, or types of rights asserted, defines the claim. *Agrilectric Power Partners, Ltd. v. Gen. Elec. Co.*, 20 F.3d 663, 665 (5th Cir. 1994). If the cases are based on the same nucleus of operative facts, the prior judgment's preclusive effect "extends to all rights the original plaintiff had 'with respect to all or any part of the

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res judicata bound Gordon Davenport to the tax court's determination of the gift tax due. The government did not waive a res judicata argument.

transaction, or series of connected transactions, out of which the [original] action arose.'" *Petro-Hunt*, 365 F.3d at 395 (citing RESTATEMENT (SECOND) OF JUDGMENTS § 24 (1)). Generally, "[t]he tax liability of a particular tax for a particular taxable year" is a single cause of action. 15 ELIZABETH K. BERMAN, MERTENS LAW OF FEDERAL INCOME TAXATION § 60: 33 (2000).

The first three elements of res judicata are not contested by the parties. As transferee, Gordon Davenport was in privity with a party to the tax court proceeding, Birnie Davenport's estate, the transferor. *See Baptiste v. Comm'r*, 29 F.3d 1533, 1539 (11th Cir. 1994) ("[I]t is well settled that a transferee is in privity with his transferor for purposes of the Internal Revenue Code."); *First Nat'l Bank of Chicago v. Comm'r*, 112 F.2d 260, 262 (7th Cir. 1940) (same). Indeed, the tax liability of the donor and donee are inseparable. A prior decision determining the liability of the donor binds the donee. 14 EDWARD J. SMITH, MERTENS LAW OF FEDERAL INCOME TAXATION § 53: 6 (2004). And the tax court, a court of competent jurisdiction, rendered final judgment on the merits.[10]

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[10] The final judgment element does not require contested litigation. "An agreed judgment is entitled to full res judicata effect." *United States v. Shanbaum*, 10 F.3d 305, 313 (5th Cir. 1994) (holding that an agreed decision in the tax court prevented the application of the innocent spouse rule in an action to enforce the tax court judgment under res judicata); *see also Matter of W. Tex. Mktg Corp.*, 12 F.3d 497, 500-01 (5th Cir. 1994) (stating that a settlement agreement between the IRS

The parties differ as to whether the fourth element of res judicata is satisfied: whether this case involves the same cause of action as the tax court proceeding. The district court, in its res judicata analysis, held that the tax court proceeding involved different operative facts than this case. The district court determined that the tax court case involved a deficiency notice against the estate itself and involved distinct facts relating to Birnie Davenport's ownership interests, donative intent, and the estate's ultimate gift tax liability, but that this case involves facts relating to donee liability and the statute of limitations under § 6324(b). The government contends, however, that the district court improperly focused on the facts litigated, as would be proper under the doctrine of collateral estoppel, rather than the operative facts of the case.

The district court's focus was improper because it looked to the legal theories advanced, forms of relief requested, and types of rights asserted. *See Agrilectric Power Partners, Ltd.*, 20 F.3d at 665. The operative facts in this case and the tax court case are identical. Both cases are based on the same two transactions and factual events: (1) the July 1980 installment sale of the Hondo stock from Birnie Davenport to Vestal and Gordon Davenport and (2) the July 1980 gift of the Hondo stock to Botefuhr. The tax court was required to decide the value of the stock to calculate the tax owed by the estate. Accordingly, under the transactional test the

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and the taxpayer incorporated into a judgment must be given full res judicata effect).

same cause of action is involved in both cases, and the district court improperly focused on what was actually litigated rather than the operative facts.

Our decision that the same cause of action is involved is consistent with the decisions of the Eighth and Eleventh Circuits that a transferee cannot relitigate the tax due after a prior court had already determined the estate's tax liability. *See Baptiste v. Comm'r*, 29 F.3d 1533, 1539 (11th Cir. 1994); *Baptiste v. Comm'r*, 29 F.3d 433, 436 (8th Cir. 1994). The *Baptiste* cases involved two brothers; Gabriel, residing in Nebraska, and Richard, residing in Florida. *See id.* Each brother received $50,000 as a beneficiary of his father's life insurance policy. *Baptiste*, 29 F.3d at 434. The IRS determined that the estate owed a deficiency in estate tax, and after the estate contested that deficiency, the IRS and the estate agreed to the estate tax owed. *Id.* The tax court entered a stipulated decision of the tax due from the estate, but the estate never paid the tax, prompting the government to attempt to collect the tax from the Baptiste brothers as transferees.[11] *Id.*

Although Gabriel Baptiste did not contest that he was personally liable as a transferee under I.R.C.

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[11] Although the *Baptiste* cases involved transferee liability with regard to an unpaid estate tax, transferee liability of estate tax functions the same as transferee liability of gift tax. Section 6324(a) of the Internal Revenue Code states that if the estate tax is not paid when due, then the transferee "who receives, or has on the date of the decedent's death, property included in the gross estate. . . to the extent of the value, at the time of the decedent's death, of such property, shall be personally liable for such tax."

§ 6324(a)(2), he attempted to contest the amount of the underlying estate tax liability in a separate proceeding in the tax court. The effort was unsuccessful, the tax court holding that res judicata applied to bar him from contesting the amount of the estate tax liability. *Id.* at 435. On appeal, Gabriel Baptiste argued that res judicata did not apply to bind him to the tax court's decision regarding the existence and amount of estate tax imposed for purposes of determining his transferee liability pursuant to § 6324(a)(2). *Id.* The Eighth Circuit held that the causes of action in the two cases were identical, that is "the transferor and Gabriel [ ] [Baptiste's] respective obligation to pay the estate tax imposed on the transfer of the decedent's estate." *Id.* at 436. Because the causes of action were identical, res judicata bound Gabriel Baptiste to the tax court's decision for purposes of determining both the transferee's obligation to pay the estate tax and the amount of the transferee's liability. *Id.* The court reasoned that the donee's liability was determined by the amount of the estate's tax. *See id.*

The Eleventh Circuit ruled similarly in the challenge brought by Richard Baptiste. *Baptiste*, 29 F.3d at 1539. Richard Baptiste wanted to relitigate the valuation of the property, but the court of appeals denied him that opportunity. *Id.* The Eleventh Circuit held that "[t]he fact that his purpose is to decrease his personal liability, rather than in the interest of the estate, is of no moment. The estate's liability under section 2002 and Baptiste's liability under section 6324(a)(2) both

embrace the same determination-the amount of estate tax imposed by chapter II." *Id.*

Gordon Davenport argues that his case can be distinguished from the Eighth and Eleventh Circuits' decisions because unlike the Baptistes, who challenged the estate's liability, he contests the extent of his own transferee liability. He contends that because the Baptiste brothers received cash, the extent of the donee's liability was fixed at the amount of the cash received and that the value of cash cannot be questioned in the way that a stock's value can be. He argues that because the Baptiste brothers could not relitigate the value of the cash (and thus the extent of their liability), they attempted to relitigate the underlying estate's liability as a means of reducing their own transferee liability.

This argument does not succeed because the value of the Hondo stock was a fundamental part of calculating the tax due in this case. The tax court's determinations of the value of the stock and the tax due are not separable. Once a court determines the tax liability of the transferor, "the decision is res judicata of the liability with regard to the transferee for the same tax if transferee status can be established." 14 EDWARD J. SMITH, MERTENS LAW OF FEDERAL INCOME TAXATION § 53: 31 (2004). The tax court concluded Gordon Davenport was a transferee, and the Tenth Circuit affirmed that decision.

Gordon Davenport also argues that we should follow the lead of the Tenth Circuit in Botefuhr, a case in which the facts were identical to those in this

case. In Botefuhr, the government attempted to assert transferee liability against Vestal to collect the tax owed by Birnie Davenport's estate. 309 F.3d at 1275. The question before the Tenth Circuit was whether Vestal was bound by the estate's stipulation during the tax court proceedings that the value of the Hondo stock was $2000 per share. *Id.* at 1281. Vestal argued that the stipulation was limited to the tax court proceeding and did not preclude litigation of that issue in the subsequent proceeding. *Id.* The Tenth Circuit acknowledged that confusion existed regarding whether the preclusion issue should be analyzed under the principles of collateral estoppel or res judicata. *Id.* at 1281-82. It concluded that "this matter must be evaluated as an assertion of [collateral estoppel], rather than [res judicata] [Res judicata] is inapplicable to the situation here presented." *Id.* The Tenth Circuit offered no other insight into its conclusion that res judicata did not apply.[12]

Although we have the utmost respect for the Tenth Circuit, we decline to follow its decision in Botefuhr that res judicata does not apply; instead, we side with the Eighth and Eleventh Circuits in the Baptiste cases. As discussed above, each element of res judicata has been satisfied in the instant case. Accordingly, the doctrine of res judicata applies to preclude Gordon Davenport and the government

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[12] Under the doctrine of collateral estoppel, the Tenth Circuit ultimately held that Vestal was not precluded from relitigating the value of the Hondo stock because it had never been litigated on the merits. *United States v. Botefuhr*, 309 F.3d 1263, 1283 (2002).

from litigating matters arising from the same nucleus of operative facts that were or could have been raised in the previous proceeding. *See Moitie*, 452 U.S. at 398.

Finally, Gordon Davenport argues that the language of the stipulation concerning the stock value was limited to the tax court proceeding and in effect the government waived res judicata with regard to that issue. His argument fails because the language does not expressly waive res judicata or express any intent regarding future proceedings. The stipulation merely states the parties' intent with regard to the proceeding in the tax court: that the Hondo stock should be valued at $2000 per share.

In conclusion, we hold that all elements of res judicata have been satisfied. Accordingly, res judicata binds Gordon Davenport to the value of the Hondo stock established in the tax court proceeding. The doctrine also precludes him from relitigating other issues that were or could have been litigated in that suit, such as whether the statute of limitations barred assessment of the gift tax on either the gift to Botefuhr or the gifts involved in the installment sale transactions. Because we hold that res judicata applies, we do not address the government's remaining arguments.

III. CONCLUSION

For the reasons discussed above, we REVERSE the district court's judgment and REMAND for further proceedings.

APPENDIX B

United States District Court, S.D. Texas,
Galveston Division.

UNITED STATES of America, Plaintiff,
v.
Gordon E. DAVENPORT, Defendant.
No. CIV.A G-03-923.

June 18, 2004.

ORDER GRANTING IN PART AND DENYING IN PART DEFENDANT'S MOTION FOR SUMMARY JUDGMENT AND GRANTING IN PART AND DENYING IN PART THE GOVERNMENT'S MOTION FOR PARTIAL SUMMARY JUDGMENT

KENT, District Judge.

When Gordon E. Davenport and his cousins received large blocks of Hondo Drilling Company stock from their financially savvy aunt, they got more than they bargained for. Confusion regarding ownership of the stock, proper valuation of the shares, and one cousin's failure to comply with the terms of a family agreement regarding payment of gift taxes, have resulted in years of litigation and the prospect of staggering financial liability to the Federal Government. The United States of America ("the United States" or "the Government") filed this lawsuit to recover unpaid gift taxes arising out of the transfer of stock from Birnie Davenport, now

deceased, to her nephews, Defendant Gordon E. Davenport ("Davenport" or "Defendant") and Charles E. Botefuhr ("Botefuhr"), and her niece Patricia L. Vestal ("Vestal"). Now before the Court come Defendant's Motion for Summary Judgment, which asserts that the Government's claims are barred by limitations, and the Government's Response and Cross Motion for Partial Summary Judgment, which seeks a determination that the Government's claims were timely asserted. For the reasons stated below, Defendant's Motion is hereby respectfully **GRANTED IN PART AND DENIED IN PART,** and the Government's Motion for Partial Summary Judgment is hereby **GRANTED IN PART AND DENIED IN PART**.

I. Background and Facts

Birnie Davenport and her older sister, Elizabeth, lived together most of their adult lives. Title to their house was held in both of their names, and they shared equally in construction and maintenance costs. Neither woman ever married, and both had long and successful careers in the oil and gas industry. Elizabeth served as an assistant to senior corporate executives, and Birnie was a legal secretary. Over the years, the two sisters commingled their earnings into a joint account and purchased assets together. Pursuant to an oral agreement between the sisters, legal title to their shared assets was in Elizabeth's name; however, they considered all investments to be jointly owned. One of their better investments was the purchase of stock in Hondo Drilling Company, a small drilling

company located in New Mexico and West Texas, and Union Supply, a related supply company. The two sisters executed wills containing identical provisions. When the first sister died, her estate would go into a testamentary trust for the benefit of the surviving sister. Upon the death of the second sister, the testamentary trust and the survivor's estate would be divided in two ways. All Hondo Drilling and Union Supply stock was to be divided into three equal shares among Davenport, Botefuhr, and Vestal. The balance of the estate was to be divided among these three cousins and two other cousins, giving a one-fifth share to each. Elizabeth Davenport died on December 2, 1979. In early 1980, her will was admitted to probate. Davenport, Botefuhr, and Vestal were appointed co-executors.

In 1980, Birnie Davenport transferred her ownership interest in 1,610 shares of stock in Hondo Drilling Co., Inc. to Defendant, Botefuhr, and Vestal. Birnie Davenport divided the stock roughly equally among the cousins, but she effected the transfers in two ways. With Davenport and Vestal, Birnie Davenport entered into sales agreements, selling 536 shares of Hondo stock to Vestal and 537 shares to Davenport.[1] The sales agreements valued the stock at $804 per share, which was the redemption price set by the directors of Hondo Drilling for the fiscal year 1980. As consideration for the stock, Davenport

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[1] This transaction also included 75 shares of Union Supply Company stock. *See* 1980 Income Tax Return, Form 6252, Defendant's Exh. 1. Because the Hondo Drilling Company stock accounted for most of the transaction's value, the Court will hereinafter refer only to the Hondo Drilling stock.

and Vestal each paid Birnie Davenport $1,000, and they executed promissory notes agreeing to pay Birnie Davenport $449,175.50 and $448,353.50, respectively, in twenty annual installments beginning in July of 1986. The sales agreements also called for annual interest on the unpaid principal.

In her 1980 Federal Income Tax Return, filed in 1981, Birnie Davenport reported these stock sales, using Form 6252 to detail the installment provisions, the subject-matter, and the fact that the sales were to related parties. *See* Form 6252, Computation of Installment Sale Income, Birnie Davenport 1980 Federal Income Tax Return, Government's Exh. 1. Less than two years after the parties entered into the sales agreements, and over four years before Davenport and Vestal were due to commence payment, Birnie Davenport forgave the balances on the notes. In March of 1983, Birnie Davenport filed a 1982 United States Gift Tax Return reporting the forgiveness of the notes, and she paid gift taxes on these gifts. *See* Government's Exh. 4, Stipulation of Facts, paras. 32-36.[2]

Unlike Davenport and Vestal, Botefuhr received his 537 shares of Hondo stock as an outright gift from Birnie Davenport in 1980. In late 1980, Botefuhr, Vestal, and Defendant signed an

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[2] Defendant does not admit that this document, which was a part of the proceedings in the Tax Court, should bind the Parties in this case, particularly as it relates to valuation of the Hondo Drilling stock. The Parties agree, however, that Birnie Davenport forgave the notes and paid gift taxes in 1982.

agreement ("the Family Agreement"), in which Botefuhr agreed to file any required gift tax returns for Birnie Davenport and also to pay any gift taxes resulting from his share of the Hondo stock.

In November 1982, the Internal Revenue Service ("IRS") sent a deficiency notice to the Estate of Elizabeth Davenport. The IRS had determined that all of the sisters' 3220 shares of Hondo stock belonged to Elizabeth Davenport's estate. In 1983, the Estate of Elizabeth Davenport petitioned the United States Tax Court to challenge this determination. The parties settled this litigation in May 1984, agreeing that half of the Hondo stock was owned by Elizabeth Davenport and that half was owned by Birnie Davenport.

Birnie Davenport died in February 1991. Defendant, Vestal, and Botefuhr were appointed personal representatives of Birnie Davenport's Estate ("the Estate"). At the time of her death, no gift tax return had been filed reflecting the 1980 gift of Hondo stock to Botefuhr. On November 7, 1991, the Estate filed a gift tax return for 1980 reporting the transfer of Hondo stock from Birnie Davenport to Botefuhr. The Estate valued the Hondo stock at $804 per share, resulting in a total tax liability of $95,322, which the Estate paid. After examining the return, the IRS determined that the Estate had understated the value of the gift to Botefuhr. The IRS also determined that Birnie Davenport had sold shares of Hondo stock to Defendant and Vestal in 1980 at a discounted rate, resulting in additional taxable gifts to them. On September 20, 1994, the IRS issued a notice of deficiency to the Estate,

asserting a gift tax deficiency of $1,422,154, as well as an addition to tax of $355,538.50 for failure to file a timely gift tax return. *See Estate of Davenport v. Commissioner*, 184 F.3d 1176, 1181 (10th Cir. 1999).

The Estate petitioned the Tax Court for a redetermination of the deficiency. On November 7, 1997, the Tax Court determined that there was a federal gift tax deficiency of $822,653 due from the Estate for the calendar year 1980 as well as an addition to tax of $205,663 for failure to file a timely gift tax return. *See id.* The Tenth Circuit affirmed the Tax Court's Decision on July 13, 1999, concluding that Birnie Davenport made taxable gifts to Defendant, Vestal, and Botefuhr during the third quarter of 1980. *See id.* at 1188. On March 2, 1998, the IRS made an assessment against the Estate for the deficiency, together with penalties and interest, and sent a notice and demand for payment to the Estate. The Estate did not pay the tax.

On February 2, 2000, the Government filed its complaint in this case in the United States District Court for the Northern District of Oklahoma. In the complaint, the Government sought (1) to reduce to judgment the liability of the Estate for the amounts due on the gift tax assessment; (2) to reduce to judgment the personal liability for unpaid gift taxes imposed upon Defendant, Vestal, and Botefuhr by 26 U.S.C. § 6324(b); and (3) judgments against the individual defendants, under 31 U.S.C. § 3713, as representatives of the Estate who had depleted its assets without satisfying the outstanding gift tax liability. The District Court asserted personal jurisdiction over Davenport and Botefuhr, both

Texas residents, because they served as personal representatives of the Estate. After both Parties filed motions for summary judgment, the defendants conceded the issue of the Estate's liability, and the Government conceded the issue of the defendants' liability as representatives of the Estate. The District Court held that section 6501 and 6502 of the Internal Revenue Code supplied the limitations period for personal liability claims against transferees under § 6324(b); therefore, the Government's claim was timely. *See United States v. Estate of Davenport,* 159 F.Supp.2d 1330 (N.D. Okla. 2001) (citing *United States v. DeGroft*, 539 F.Supp. 42, 44 (D.Md. 1981)). The Tenth Circuit reversed the District Court's ruling on personal jurisdiction over Botefuhr and Davenport but affirmed the statute of limitations issue, holding that the limitations period established by § 6502(a) governs individual liability claims under § 6324(b) and that the Government's claim was timely against Vestal. *See United States v. Botefuhr*, 309 F.3d 1263 (10th Cir. 2002). The Tenth Circuit remanded for determination of the value of the Hondo stock on the date of the gift.

On remand, the District Court transferred the Government's action against Defendant Gordon E. Davenport to this Court. On March 5, 2004, Defendant filed his Motion for Summary Judgment, arguing that the Government's claims are untimely. On April 8, 2004, the United States filed its Opposition and Cross Motion for Partial Summary Judgment, seeking a determination that its assessment and collection actions were timely

commenced against Defendant.

II. Legal Standard

Summary judgment is appropriate if no genuine issue of material fact exists, and the moving party is entitled to judgment as a matter of law. *See* Fed.R.Civ.P. 56(c); *see also Celotex Corp. v. Catrett*, 477 U.S. 317, 323, 106 S.Ct. 2548, 2552-53, 91 L.Ed.2d 265 (1986). When one party moves for summary judgment, the nonmoving party must set forth specific facts showing that there is a genuine issue for trial. *See Anderson v. Liberty Lobby, Inc.*, 477 U.S. 242, 250, 106 S.Ct. 2505, 2510, 91 L.Ed.2d 202 (1986). Issues of material fact are "genuine" only if they require resolution by a trier of fact. *See id.* at 248, 106 S.Ct. at 2510. The mere existence of some alleged factual dispute between the parties will not defeat an otherwise properly supported motion for summary judgment; rather, only disputes over facts that might affect the outcome of the lawsuit under governing law will preclude the entry of summary judgment. *See id.* at 247-48, 106 S.Ct. at 2510. Nevertheless, if the evidence is such that a reasonable fact-finder could find in favor of the nonmoving party, summary judgment should not be granted. *See id.; see also Matsushita Elec. Indus. Co. v. Zenith Radio Corp.*, 475 U.S. 574, 587, 106 S.Ct. 1348, 1356, 89 L.Ed.2d 538 (1986). Determining credibility, weighing evidence, and drawing reasonable inferences are left to the trier of fact. *See Anderson*, 477 U.S. at 255, 106 S.Ct. 2505, 2513.

III. Analysis

The Government seeks to collect the Estate's unpaid gift taxes from Defendant through the transferee liability provision of 26 U.S.C. § 6324(b). Under the Internal Revenue Code, a transfer of property by gift in any calendar year is subject to tax for that calendar year. *See* 26 U.S.C. § 2501(a). The donor of the gift must file a gift tax return and pay the gift tax on all taxable gifts made in that year. *Id.* § 2502(c); *id.* § 6019 If the donor dies before filing the return and paying the gift tax, the executor or administrator of the estate must file the return, and the estate must pay the tax. *See* 26 C.F.R. §§ 25.2502-2.6019-1(g). If the gift tax is not paid by the donor when due, "the donee of any gift shall be personally liable for such tax to the extent of the value of such gift." 26 U.S.C. § 6324(b). Section 6324(b) also provides that the unpaid tax "shall be a lien upon all gifts made during the period for which the return was filed, for 10 years from the date the gifts are made." *Id.*

The IRS must assess the amount of any tax due within three years after the relevant return is filed. *See* 26 U.S.C. § 6501(a). The Government characterizes an "assessment" as essentially an internal bookkeeping procedure used to record the amount of a taxpayer's liability in the IRS records. *See* 26 U.S.C. § 6203; *Laing v. United States*, 423 U.S. 161, 170 n. 13, 96 S.Ct. 473, 479, 46 L.Ed.2d 416 (1976). Following a timely assessment, the IRS may collect the tax due by levy or by a court proceeding, but the levy or proceeding must begin

within 10 years of the assessment. *See id.* § 6502(a).

The Government asserts that it made a timely assessment of tax liability against the Estate pursuant to § 6502(a); therefore, its claim against Defendant is timely because it was brought within ten years of the assessment. *See id.* Defendant argues that the Government's claim under § 6324(b) is untimely for three reasons. First, Defendant asserts that personal liability under § 6324(b) expires with the ten-year lien. Second, Defendant argues that the Government's failure to make an assessment against Defendant as transferee bars the claim under § 6324(b). Finally, Defendant argues that even under the limitations period suggested by the Government, its claims are untimely insofar as they are based on the 1980 installment sale because the Government had complete notice of that transaction in 1981.

Because the Court agrees with the Tenth Circuit and the Northern District of Oklahoma that the general limitations in sections 6501 and 6502 apply to personal liability claims under 6324(b), the Court finds that the Government's claims are timely to the extent that they arise out of unpaid gift taxes assessed within three years of the Estate's filing of its 1980 Gift Tax Return. The Tax Court ruled that the deficiency notice, issued on September 20, 1994, served as a timely assessment of the tax owing from the Gift Tax Return filed in 1991. There remains a dispute, however, regarding the scope of this assessment, timely though it may have been. Because the Court finds that the Government had notice of the 1980 installment sale to Defendant in

1981, the Government's 1994 assessment was not timely with respect to gift taxes arising out of that transaction. Because the Government failed to timely assess the taxes owing on the imputed gift element of the installment sale, the claim for the taxes arising out of the imputed gift to Gordon Davenport is barred by limitations.

A. The Limitations Period in § 6502(a) Applies to Claims Brought Pursuant to § 6324(b)

Defendant maintains that personal liability under § 6324(b) is subject to the same ten-year limit as the special lien. The Government has conceded that the period for enforcing the special lien has lapsed. *See Botefuhr,* 309 F.3d at 1277 (citing *Estate of Birnie Davenport*, 159 F.Supp.2d at 1333). As the Tenth Circuit noted, however, § 6324(b) distinguishes between the special lien and the transferee's personal liability. *See id.* The latter provision contains no statute of limitations. Because the statute clearly makes personal liability under § 6324(b) independent from the ten-year lien, the Court agrees with the Tenth Circuit that the special lien does not establish a limitation period for the personal liability of the transferee. *See id.*

Nor does the Government's failure to make an assessment against Defendant as transferee prevent it from pursuing a personal liability claim under § 6324(b). Defendant's argument for a transferee assessment is based on § 6901, which requires that the amount of the liability of a transferee shall be "assessed, paid, and collected in the same manner and subject to the same provisions and limitations as

in the case of the taxes with respect to which the liabilities were incurred." 26 U.S.C. § 6901. Numerous courts have held, however, that a transferee assessment under § 6901 is not a prerequisite to a personal liability suit under 26 U.S.C. § 6324(a)(2), which imposes liability on the transferees of a decedent's estate when the estate fails to pay its taxes. *See United States v. Geniviva*, 16 F.3d 522, 524 (3d Cir. 1994) (explaining that § 6324 predates § 6901, which, rather than eliminating the remedy provided by § 6324, merely provides an additional method of tax collection); *United States v. Russell*, 461 F.2d 605 (10th Cir. 1972) (holding that "the collection procedures of § 6901 are cumulative and alternative-not exclusive or mandatory"); *United States v. Estate of Davenport*, 159 F.Supp.2d 1330, 1335 (N.D. Okla. 2001), *rev'd in part on other grounds, United States v. Botefuhr*, 309 F.3d 1263 (10th Cir. 2002). While *Geniviva* and *Russell* arose out of the Government's attempt to collect delinquent estate taxes from transferees under § 6324(a), it is well-established that the gift tax and estate tax provisions of §6324 "are in *pari materia* and must be construed together." *Estate of Sanford v. Commissioner*, 308 U.S. 39, 44, 60 S.Ct. 51, 84 L.Ed. 20 (1939), *cited in Botefuhr*, 309 F.3d at 1276 n.9. Based on this authority, the Court agrees that a personal liability claim under §6324(b) may be brought without a prior assessment against the transferee under § 6901.

The question remains what limitations period applies to the Government's claim. In *Botefuhr*, the Tenth Circuit noted that although few courts have

considered this issue, those that have done so have looked to the general limitations provisions in sections 6501 and 6502. *See Botefuhr,* 309 F.3d at 1277. This reliance on sections 6501 and 6502 is based on the theory that "so long as the government could bring a timely action against the donor, its action against the donee will be considered timely." *Id.*; *see also United States v. Wright*, 57 F.3d 561, 564 (7th Cir. 1995). ("[S]uits against persons derivatively liable for taxes are timely, or not, according to the rules for timeliness of suits against taxpayers."). The Court agrees with the Tenth Circuit's interpretation, which harmonizes § 6324(b)'s personal liability provision with other relevant code provisions while preserving the distinction between primary donor liability and derivative personal liability under 6324(b). Once the Government has timely assessed the gift tax against the donor, the same ten-year limitations period applies to the donor and donee under § 6502(a).

Defendant argues in the alternative that even if § 6501 requires an assessment against the transferor only, § 6502 cannot supply the limitations provision for a § 6324(b) claim because it is triggered by an assessment. In Defendant's view, this is inconsistent with the self-actuating nature of the transferee's personal liability under § 6324(b). The Court disagrees. The mere fact that § 6501 requires an assessment against the transferor does not affect the "no-assessment" aspect of § 6324(b). Because the latter provision concerns transferees only, its purpose would only be contravened by a requirement that the IRS make an assessment against the

transferee. The assessment required by § 6501 secures the Government's ability to collect the gift tax liability from the transferor. Its only effect upon the transferee's derivative, non-tax liability under § 6324(b) is to establish a time limit for enforcement.

To summarize, claims against a transferee under § 6324(b) must be brought within the period prescribed by sections 6501 and 6502. Section 6501 requires that the Government assess any tax imposed within three years of the date the return was filed. 26 U.S.C. § 6501(a). Section 6502 provides that once a timely assessment has been made, the tax may be collected within ten years after the assessment of the tax. 26 U.S.C. § 6502(a)(1). The determination that § 6324(b) is governed by the three-year assessment provision of § 6501 and the ten-year limitations period of § 6502 settles the question whether the Government timely filed its claims arising out of the 1980 gift of Hondo Drilling stock to Botefuhr. The Government issued a notice of deficiency, which was determined by the Tax Court to be the equivalent of an assessment, within three years of the Estate's filing of the 1980 Gift Tax Return. The Tenth Circuit's decision in *Botefuhr* makes clear that § 6324 imposes liability on a donee "for *any* gift tax incurred by the donor during the year in which the donee received a gift, *regardless of whether* that individual donee's gift actually contributed to the donor's gift tax deficiency." *Botefuhr*, 309 F.3d at 1276 (citing *Want v. Commissioner*, 280 F.2d 777, 781 (2d Cir. 1960) (Friendly, J.); *La Fortune v. Commissioner*, 263 F.2d 186, 194 (10th Cir. 1958)). Defendant may therefore

be liable for the unpaid gift taxes resulting from Birnie Davenport's gifts to his cousins, even if the Government is barred from collecting taxes on his own gift.

B. The IRS Had Sufficient Notice in 1981 to Trigger the Statute of Limitations on Claims Arising out of the Installment Sale

Defendant argues that the 1980 income tax return filed by Birnie Davenport in 1981 provided the Government with sufficient notice of the imputed gift of Hondo Drilling stock to trigger the statute of limitations on any claim arising out of that gift.[3] The Government maintains that it did not receive sufficient notice of the imputed gift in the 1980 installment sale transaction between Birnie and Gordon Davenport until the Estate filed its 1980 Gift

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[3] Patricia Vestal made a similar argument before the Tenth Circuit, but the Circuit deemed the argument waived for failure to raise it in the district court. *See Botefuhr*, 309 F.3d at 1280 n. 14 (declining to consider the argument because it was raised for the first time in the reply brief on appeal). Davenport has properly and timely raised the argument in this proceeding.

Vestal also argued that Birnie Davenport's gift tax return of March 31, 1983, which reflected the forgiveness of the promissory notes executed by Vestal and Davenport, provided sufficient notice to start the statute of limitations on any claims to collect taxes arising out of the installment sale transactions. *See id.* at 1279. The Tenth Circuit declined to consider this argument, noting that Vestal failed to raise it in the district court. The Court also noted that the 1980 installment sale and the forgiveness of the promissory note in 1982 constituted separate gifts. *See id.* at 1280 n. 12. Defendant does not base his notice argument upon Birnie Davenport's 1983 gift tax return.

Tax Return in 1991. Because Birnie Davenport's 1981 Income Tax Return provided complete notice of the installment sale, and because the 1980 Income Tax Return that the Estate filed in 1980 provided no additional notice of the transaction, the Court concludes that the Government had sufficient notice of the gift to Defendant in 1981. Because the Government failed to assess the tax arising out of this gift within three years of the filing of the Income Tax Return as required by 26 U.S.C. § 6501, its claim against Defendant pursuant to § 6324(b) is not timely as it relates to the installment sale.

The Tenth Circuit recognized in *Botefuhr* that "once [a] taxpayer has evinced an honest and genuine effort to satisfy the law by filing such a return, the § 6501(a) period begins to run." 309 F.3d at 1279. The issue of notice turns on the question whether Birnie Davenport's 1980 Income Tax Return, which specifically listed the sales agreements and designated them as related-party transactions, constitutes an honest and genuine effort to satisfy the law. That the Parties talk past each other on this point may perhaps be explained by the anomalous nature, at least for purposes of reporting, of an "imputed gift." Obviously, the Government takes the position that Birnie Davenport made a taxable gift to Defendant in late 1980. Although Defendant no doubt disagrees with this conclusion, the Tax Court's decision that such a gift was made resolves the question for purposes of this litigation. But this fundamental dispute highlights a crucial fact: It is inherent in the concept of an imputed gift that the parties to the

original transaction do not share the Government's opinion that the transaction involves a gift. Given this basic assumption, to expect the would-be taxpayer to file a gift tax return makes little sense. Considering that the taxpayer does not perceive that he or she has made a gift at all, the most that might reasonably be expected is that she would report the sale proceeds as income on her income tax return.[4]

The record indicates that these assumptions are borne out in the real world. In her 1980 Income Tax Return, Birnie Davenport filled out a special form, Form 6252, to report her income from the installment sale to Defendant. *See* Form 6252, Government's Exh. 1. Item D in Form 6252 asks whether the property at issue was sold to a related party; Birnie Davenport marked "Yes." *See id.* "The presumption is that a transfer between closely related parties is a gift." *Estate of Reynolds v. Comm'r*, 55 T.C. 172, 201, 1970 WL 2324 (1970); *see also Wheeler v. United States*, 116 F.3d 749, 763 (5th Cir. 1997). It seems logical to assume that this presumption rests on the understanding that a transaction between related parties that does not

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[4] The Internal Revenue Code does grant the Government unlimited time to collect taxes in cases involving false or fraudulent returns: "In the case of a false or fraudulent return with the intent to evade tax, the tax may be assessed, or a proceeding in court for collection of such tax may be begun without assessment, at any time." 26 U.S.C. § 6501(c)(1). However, the Government does not argue that Birnie Davenport, the Estate, or Defendant made such an attempt, nor does the Court find evidence in the record to support such a finding.

bear the normal features of a gift-that is, the kind of transaction in which the IRS would likely find an imputed gift element-would not likely be reported by the parties as a gift.

The Government states that, after examining the 1980 Gift Tax Return filed by the Estate, it determined that Birnie Davenport had also sold shares of the Hondo stock to Vestal and Davenport at a discounted rate in 1980, resulting in taxable gifts. United States' Opposition and Cross Motion for Partial Summary Judgment at 7. If the government had received no prior notice that the 1980 installment sale took place, and if the Estate's 1980 Income Tax Return had in fact drawn the Government's attention to that transaction, the Court would agree that proper notice did not occur until 1991. But the Court sees no evidence that the 1980 Gift Tax Return, filed in 1991, provided any notice of the decedent's transactions with Defendant or Vestal. Indeed, the prior rounds of this controversy indicate that the 1980 Gift Tax Return provided the Government with information about the gift to Botefuhr only. *See Estate of Davenport*, 184 F.3d at 1180 (finding that the Estate "prepared a gift tax return reflecting a gift of 537 shares of Hondo stock in the third quarter of 1980 from Birnie to Mr. Botefuhr"). While it may have encouraged the Government to check Birnie Davenport's file for 1980, the Gift Tax Return provided no information whatsoever regarding Birnie Davenport's transaction with Defendant. The Government's determination that additional taxable gifts occurred in 1980 may have been made *after* it received the

1980 Gift Tax Return, but that determination could not have been made *because of* the gift tax return. The information simply wasn't there. The only document in the record that provides information about the imputed gift to Defendant is Form 6252 in Birnie Davenport's 1980 Income Tax Return. Thus, all of the information that the IRS needed-and all of the information it now relies upon-to collect the taxes on Birnie Davenport's 1980 gift to Defendant, it had in 1981. Indeed, all the notice the Government *ever received* came to it through Birnie Davenport's 1980 Income Tax Return.[5]

The Government stresses that the limitations period does not begin until the actual filing of the gift tax return. Given the nature of imputed gifts,

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[5] The Government advances a number of arguments based on the theory that Birnie Davenport's 1980 gift to Defendant-the undervalued installment sale-was reflected in the 1980 Gift Tax Return filed on behalf of the Estate in 1991. For example, the Government asks, "If the executors of the Birnie Davenport Estate believed they had done all that was necessary in respect to the stock transfers prior to Birnie Davenport's death, why did they file the delinquent gift tax return in 1991?" Response at 16. There is no evidence in the record, however, of any nexus between Birnie Davenport's gift to Defendant and the Estate's 1980 Gift Tax Return. To the contrary, and as explained above, the record indicates that the Estate's gift tax return mentioned only the gift to Botefuhr. Defendant's action in filing this return as a representative of Birnie Davenport's Estate does not constitute an admission or acknowledgment of his own donee liability arising out of the 1980 installment sale, which was an entirely separate transaction. Any argument by the Government to this effect is based on a faulty premise that is not supported by the record.

the Government's position would require the Court to hold that claims against a taxpayer or transferee for imputed gifts are not subject to any limitations period. At least in situations like the current one, where the taxpayer made a good faith effort to report the transaction in full on a timely filed tax return, including information that the parties were related, this simply cannot be the case.

Because Birnie Davenport made an honest effort in her 1980 Income Tax Return to report the transaction that gave rise to the Government's current claims against Defendant, and because the Government relies upon no other source for information regarding that transaction, the Court finds that the 1980 Income Tax Return constitutes a reasonable and honest effort to comply with the law. Moreover, because the Income Tax Return alone provided notice to the Government that Birnie Davenport should have paid gift taxes on the installment sale of Hondo Drilling stock to Defendant, the Court finds that the Government had adequate notice of Birnie Davenport's gift to Defendant in 1981. Under the limitations framework discussed above, the Government was required to assess the tax on the gift to Defendant within three years after the 1980 Income Tax Return was filed. Because it failed to do so, no timely assessment was made, and its claim is barred to the extent that it seeks taxes arising out of the 1980 installment sale of Hondo Drilling stock from Birnie Davenport to Defendant. The Court recognizes the Supreme Court's longstanding admonition that "[s]tatutes of limitation sought to be applied to bar

rights of the Government, must receive a strict construction in favor of the Government." *Badaracco v. Commissioner*, 464 U.S. 386, 391, 104 S.Ct. 756, 761, 78 L.Ed.2d 549 (1984) (citing *E.I. Dupont De Nemours & Co. v. Davis*, 264 U.S. 456, 462, 44 S.Ct. 364, 366, 68 L.Ed. 788 (1924)). Indeed, the Court has historically gone to extraordinary lengths to assist the Government in its efforts to enforce the tax laws, even going so far, on several occasions, as to report the failure of certain personal injury claimants to pay income tax for years on end. Nonetheless, based on *this* record, which the Parties have had years to develop, the Court cannot conceive of a reasonable construction of the law that would permit the Government to pursue its claim for taxes arising out of the 1980 sale of Hondo Drilling stock to Defendant. On this ground only, Defendant's Motion for Summary Judgment is **GRANTED**, and the Government's Motion for Partial Summary Judgment is hereby respectfully **DENIED**.

IV. Conclusion

For the reasons stated above, the Court concludes that the United States' assessment and collection actions to recover unpaid gift taxes against Defendant Gordon Davenport are timely insofar as they seek to collect unpaid taxes on the gift of 537 shares of Hondo Drilling Co. stock from Birnie Davenport to Charles E. Botefuhr in 1980. Therefore, as to the claims arising out of the 1980 gift to Botefuhr, Defendant's Motion for Summary Judgment is hereby respectfully **DENIED**, and the United States' Cross Motion for Partial Summary

Judgment is hereby **GRANTED**. However, because the United States failed to timely assess the taxes arising out of the installment sale of Hondo Drilling Company stock to Defendant Gordon Davenport, the Government's claim to collect such taxes is barred by limitations. Accordingly, as to the claims arising out of the taxes on Birnie Davenport's 1980 gift to Defendant Gordon E. Davenport, Defendant's Motion is hereby **GRANTED**, the Government's Motion is hereby respectfully **DENIED**, and such claim is hereby respectfully **DISMISSED WITH PREJUDICE**. A Final Judgment in this regard will be entered in due course. Each Party is to bear its own taxable costs, attorneys' fees, and expenses incurred herein to date.

IT IS SO ORDERED.

APPENDIX C

United States District Court, S.D. Texas,
Galveston Division.

UNITED STATES of America, Plaintiff,
v.
Gordon E. DAVENPORT, Defendant.
No. CIV.A G-03-923.

February 22, 2005.

REPORT AND RECOMMENDATION

Before the Court by referral from the District Court are Defendant Gordon Davenport's ("Davenport") Second Motion for Summary Judgment and Plaintiff's ("the United States" or "the Government") Cross-Motion for Partial Summary Judgment. Having carefully examined the parties' Motions and the record in this case, the Court submits its Report and Recommendation to the District Court. In light of the District Court's thorough discussion of the facts that led up to this case and the legal issues involved in a donee's liability under the Internal Revenue Code, the Court foregoes a detailed examination of these matters. This Report incorporates by reference the District Court's prior discussion of these issues.

In 1997, a United States tax court determined that the estate of Davenport's late aunt, Birnie Davenport, owed the Government a gift tax deficiency of $1,422,154. *Estate of Davenport v.*

Commissioner, T.C. Memo 1997-390. The Tenth Circuit affirmed the tax court's decision. *Davenport v. Commissioner*, 184 F.3d 1176 (10th Cir. 1999). The Government then filed suit in the Northern District of Oklahoma to reduce the tax court's decision to judgment. The suit was brought against Davenport and his two cousins, Patricia Vestal ("Vestal") and Charles Botefuhr ("Botefuhr"), individually and in their capacities as co-personal representatives of their aunt's estate ("the Estate"). The District Court granted summary judgment for the Government, but the Tenth Circuit reversed the decision in part and found that the Oklahoma court lacked personal jurisdiction over Davenport and Botefuhr. *United States v. Botefuhr*, 309 F.3d 1263 (10th Cir. 2002). The case was remanded for further determination on those portions of the District Court's decision that were reversed, and the actions against Davenport and Botefuhr were transferred to this Division and to the Western District of Texas, respectively.

The Government's action in the Oklahoma court sought to collect the Estate's unpaid gift taxes on three separate gifts of stock of Hondo Drilling Co. Inc. ("Hondo") made to Davenport, Vestal, and Botefuhr in 1980. The gift to Botefuhr was made by direct transfer. Botefuhr agreed to file a gift tax return on the gift and pay any tax owed on it. He did not do so, and the Estate filed the required return for the 1980 gift only when it discovered in 1991 that Botefuhr had not kept his promise. The transfers to Davenport and Vestal were each made through a sales agreement that valued the Hondo

shares at $804 per share, the price set for redemption by Hondo in 1980. Each transferee paid $1,000 and executed a promissory note agreeing to pay their aunt the value of their stock. For Davenport, this amounted to $449,175. Payment was not to begin, however, until July, 1986. Two years after the transfer, Birnie Davenport forgave the balances owed on the notes, filed a gift tax return reporting that forgiveness, and paid gift taxes in the amount of $71,911.

The Government sought payment from Davenport for additional taxes owed on the gift of stock made to him. The Government also seeks payment from Davenport for the taxes owed on the gift made to Botefuhr. In an earlier ruling, the District Court determined that the Government's claim for taxes owed on the imputed gift to Davenport himself was barred by the applicable statute of limitations. Under the transferee liability provision of 26 U.S.C. § 6324(b), a donee is liable up to the extent of the value of his own gift for *any* gift tax incurred by the donor during the year in which the donee received his gift. This is true regardless of whether or not the defendant/donee's gift contributed to the gift tax deficiency. *La Fortune v. Commissioner,* 263 F.2d 186, 194 (10th Cir. 1958). The District Court held that the Government's claim against Davenport for taxes owed by Botefuhr is timely. *United States v. Davenport,* 327 F. Supp.2d 725 (S.D. Tex. 2004)(Kent, J.). The Government now seeks judgment for those taxes.

Davenport argues that he is not liable for any gift taxes because he cannot be deemed to ever have

been the donee of a gift. In doing so, he relies on two aspects of the prior litigation involving the Estate. In the 1997 tax court case, the court noted that the parties stipulated that the fair market value of the Hondo stock at the time of transfer in 1980 was $2,000 per share, not the $804 that was stated in the sales agreement or by Hondo as the redemption price. The Government argued to the Tenth Circuit, as it does here, that this stipulation is binding on subsequent litigation. The Tenth Circuit rejected this argument in relation to Vestal. *Botefuhr*, 309 F.3d at 1281-82. Davenport now claims that, in the absence of the $2,000 per share stipulation, the 1980 transfer of stock to him under the installment agreement was a purchase, not a gift. According to him, unless it can be established that the stock's value exceeded $804 per share, it cannot be an imputed gift because Birnie herself paid gift taxes on the forgiveness of his debt under the installment notes.

However, the value of the 1980 transfer of Hondo stock to Davenport himself is not at issue any longer because the District Court has already found that the Government's claim on that specific transfer is barred by the statute of limitations. The only issue remaining is the Government's claim against Davenport for the unpaid taxes on the 1980 transfer to Botefuhr. Davenport's claim appears to be that, if he himself did not receive a gift from Birnie in 1980, he cannot be a donee liable for the unpaid gift tax on Botefuhr's gift made in the same year.

At the heart of both parties' Motions is the issue of what binding effect the tax court's ruling has

on this Court. The Government argues that the stipulation made between the Estate and the Commissioner that the Hondo stock was worth $2,000 a share is mandatory under the doctrine of collateral estoppel, also known as issue preclusion. In order to demonstrate collateral estoppel, the Government must show that: (1) the issue under consideration is identical to that litigated in tax court; (2) it was "fully and vigorously litigated" there; (3) it was necessary to support the tax court's decision; and (4) there are no special circumstances that would make it unfair to apply the doctrine. *Winters v. Diamond Shamrock Chern. Co.*, 149 F.3d 387, 391 (5th Cir. 1998).

The Tenth Circuit rejected the Government's issue preclusion claim, and this Court agrees with its reasoning. The value of the Hondo stock was stipulated in the prior proceeding; it was not litigated on its merits. "Generally speaking, when a particular fact is established not by judicial resolution but by stipulation by the parties, that fact has not been 'actually litigated' and thus is not a proper candidate for issue preclusion." *Botefuhr,* 309 F.3d at 1282 (quoting *Otherson v. Dep't of Justice,* 711 F.2d 267, 274 (D.C. Cir. 1983)); *see also Restatement (Second) of Judgments* § 27 cmt. 3 at 256-57 (1982) (stating that a stipulation does not qualify for actual litigation between the parties). The Fifth Circuit has echoed this sentiment. "When one party to a tax case concedes or stipulates the issue upon which the court bases its judgment, the issue is not conclusively determined for purposes of collateral estoppel unless it appears clear that the

parties so intended." *Anderson, Clayton & Co. v. United States,* 562 F.2d 972, 992 (5th Cir. 1977). As the Circuit has noted, the "actually litigated" factor in the test for issue preclusion does not require a trial, but it does demand "that the issue [be] raised, contested by the parties, submitted for determination by the court, and determined." *In the Matter of Keaty*, 2005 WL 57312 at *5 (5th Cir. Jan 12, 2005).

In this case, the question of valuation was not submitted to the tax court for decision. The court stated that the issues before it were whether: (1) Birnie owned the stock in her lifetime; (2) she made an *inter vivos* transfer of it to Davenport, Vestal, and Botefuhr in 1980; (3) the transfer constituted a gift for federal gift tax purposes; (4) the 1980 gift tax return was timely; and (5) the limitations period for assessing a gift tax deficiency had expired. *Estate of Davenport*, T.C.M. 1997390. The stipulation itself reads: "For purposes of this litigation, if the court finds that Birnie Davenport transferred Hondo stock to [the recipients] ... the parties agree that the fair market value of such Hondo stock was $2,000 per share at the time of the transfers." Stipulation at ¶ 38.

Although a stipulation can be preclusive if the parties manifest an intention to that effect, the language of the 1997 agreement is unclear as to how far it extends. *See Restatement (Second) of Judgments* § 27 cmt. e at 257; Wright, Miller & Cooper, *18 Federal Practice & Procedure* § 4443 at 252-53 (2d ed. 2002) ("issue preclusion ordinarily does not attach unless it is clearly shown that the

parties intended that the issue be foreclosed in other litigation."). The parties may *have* intended this to be limited to the specific tax court case at hand, or they may also have intended "this litigation" to extend to a subsequent action in federal court to enforce the tax court's judgment.

The Government has pointed to no evidence suggesting that the parties intended this language to extend *beyond* the tax court case itself. As Davenport points out, the stipulation has not had *any* preclusive effect on Botefuhr, who has come to an agreement with the Government in a related case that his 1980 gift of Hondo stock should be valued at $2,190 per share. Davenport's Reply at Ex. 1. While the new settlement agreement is not governing in the instant proceeding, it is a further sign that the parties to the 1997 stipulation did not intend to be bound by the $2,000 per share value beyond the limited proceeding in tax court.

Further, the $2,000 per share stipulation does not form the basis for the tax court's ruling on the five issues actually litigated. The court's determination of the issues before it depended on construing Oklahoma property law, state law governing a completed gift, and statutory limitations language. None of the court's determinations of the issues specifically raised *depended* on the valuation stipulation, which is only mentioned in a footnote. *See Estate of Davenport*, T.C.M. 1997390. The Court therefore agrees with the Tenth Circuit that collateral estoppel does not make the 1997 stipulation binding at this point.

The Tenth Circuit also held without explanation that claim preclusion, or true res judicata, does not apply to this case. *Botefuhr*, 309 F.3d at 1282. Claim preclusion requires a showing of four elements: (1) the parties in the later action must be identical to, or in privity with, *those* in the prior one; (2) the previous judgment was made by a court of competent jurisdiction; (3) the prior decision must have concluded with a final judgment on the merits; and (4) the same claim or cause of action must have been involved in both actions. *United States v. Shanbaum*, 10 F.3d 305, 310 (5th Cir. 1994). The Tenth Circuit combines the second and third elements in its test for claim preclusion. *Yapp v. Excel Corp.*, 186 F.3d 1222, 1227 (10th Cir. 1999). As a transferee, Vestal was in privity with the Estate. *Baptiste v. Commissioner*, 29 F.3d 1533, 1538 (11th Cir. 1994). Therefore, since the tax court's ruling was clearly a final judgment issued by a court of competent jurisdiction, the Circuit must have decided that claim preclusion did not apply to Vestal based on the fourth factor.

This Court agrees with the Tenth Circuit. The Fifth Circuit has adopted a transactional test for deciding whether two complaints involve the same cause of action. The important issue is whether the two actions are based on the same nucleus of operative facts. *Agrielectric Power Partners, Ltd. v. General Electric Co.*, 20 F.3d 663, 665 (5th Cir. 1994). The tax court case involved a deficiency notice against the Estate itself and involved facts relating to Birnie's ownership interests, donative intent, and the Estate's ultimate gift tax liability.

The Government argues that Davenport is merely attempting to re-litigate the Estate's tax liability. He is not. The Oklahoma District Court case sought to enforce the assessment, not only against the Estate, but also against the donees in their individual capacities. *United States v. Estate of Davenport,* 159 F. Supp.2d 1330 (N.D. Okla. 2001). Davenport does not argue that the Estate is not liable; his position is that he has no personal liability. Unlike in the tax court case, the District Court case involved facts relating to donee liability and the applicable statute of limitations under § 6324(b). None of the facts that were critical to the tax court's decision were discussed in the Oklahoma federal case, which involved interpretation of a statute that was not at issue in tax court. Nor did the Commissioner claim in the tax court case that it sought payment from Davenport for Botefuhr's gift tax deficiency. Thus, the valuation stipulation in tax court is not binding on Davenport at this point under issue or claim preclusion.

Davenport's second claim that the tax court did not establish that he is the donee of the Hondo stock is foreclosed by both claim and issue preclusion. Unlike the valuation issue, the tax court heard specific arguments from the parties as to what ownership Birnie had in the stock and whether she made a gift to Davenport, Vestal, and Botefuhr in 1980. It concluded that "Birnie did make a completed gift of Hondo stock in July of 1980" and upheld the Commissioner's finding that a taxable gift had been made. *Estate of Davenport,* T.C.M. 1007-390. In deciding that Birnie was a donor who

made a taxable gift to Davenport in 1980, the tax court necessarily found that Davenport was a donee and "in privity" with the Estate. Res judicata extends to elements that are presupposed by a tax court's decision, *Teal v. Internal Revenue Service*, 16 F.3d 619, 621 (5th Cir. 1994), and Davenport is therefore bound by the tax court determination that he is a donee.

For these reasons, the Court **RECOMMENDS** that Defendant's Second Motion for Summary Judgment (Instrument No. 137) and Plaintiff's Cross-Motion for Partial Summary Judgment (Instrument No. 139) be **GRANTED IN PART AND DENIED IN PART**.

The Clerk shall send copies of this Report and Recommendation to the parties by the means in place for transmission of same. The parties shall have until **March 4, 2005**, to have written objections, filed pursuant to 28 U.S.C. § 636(b)(1)(C), **physically on file** in the Office of the Clerk. The Objections shall be mailed to the Clerk's Office in Galveston, Texas 77553 at P.O. Drawer 2300. **Any Objections filed shall be contained in a written document specifically entitled "Objections to the Report and Recommendation of the Magistrate Judge"**, which will then be forwarded to the District Judge for consideration. Failure to file written objections within the prescribed time shall bar the aggrieved party from attacking on appeal the factual findings and legal conclusions accepted by the District Judge, except upon grounds of plain error.

DONE at Galveston, Texas, this 18th day of February, 2005.

s/John R. Froeschner
John R. Froeschner
United States Magistrate Judge

APPENDIX D

United States District Court, S.D. Texas,
Galveston Division.

UNITED STATES of America, Plaintiff,
v.
Gordon E. DAVENPORT, Defendant.
No. CIV.A G-03-923.

March 16, 2005.

ORDER

Before the Court are the Objections to the Magistrate Judge's Report and Recommendation timely filed by the United States of America ("the Government") and by Defendant Gordon Davenport.

The Government objects to the Magistrate Judge's finding that neither issue preclusion nor res judicata applies to a stipulation concerning the valuation of stock made in a prior proceeding in Tax Court. This Court agrees with the Magistrate Judge and the Tenth Circuit, which ruled on the same issues regarding a co-representative of the estate in question, for the reasons stated in the Report and Recommendation. The Court also finds that judicial estoppel does not apply.

Davenport objects to the Magistrate Judge's rejection of his claim that no imputed gift was ever made from Birnie Davenport to him. Again, the Court disagrees for the reasons stated in the Report and Recommendation.

Therefore, it is **ORDERED** that Defendant's Second Motion for Summary Judgment (Instrument No. 137) and Plaintiff's Cross-Motion for Partial Summary Judgment (Instrument No. 139) are both **GRANTED IN PART AND DENIED IN PART**.

This case is referred back to the Magistrate Judge for further proceedings.

DONE at Galveston, Texas this 15th day of March, 2005.

s/Samuel B. Kent
Samuel B. Kent
United States District Judge

APPENDIX E

United States District Court, S.D. Texas,
Galveston Division.

UNITED STATES OF AMERICA
v.
Gordon E. DAVENPORT
No. Civ.A. G-03-923.

Jan. 18, 2006.

OPINION AND ORDER

FROESCHNER, Magistrate J.

Before the Court is the "Third Motion for Summary Judgment" of Defendant, Gordon E. Davenport. Having carefully considered the Parties' numerous submissions and legal arguments, the Court is of the Opinion that the Government has no admissible evidence to prove the amount of its damages and that the Motion for Summary Judgment must be granted.

Summary Judgment is appropriate when a Plaintiff fails to establish the existence of an element essential to its case upon which the Plaintiff has the burden of proof at trial. *Celotex Corp. v. Catrett*, 477 U.S. 317, 322, 106 S.Ct. 2548, 91 L.Ed.2d 265 (1986) In the instant case the Government bears the burden of proving its damages and its damages are an essential element of its claim for unpaid gift taxes. Unfortunately, for the Government, all of the

evidence it proposes to introduce at trial to prove the per-share value of the 1,610 shares of Hondo stock on July 2, 1980, the date it was given to Davenport by his Aunt Birnie, is, for one or more reasons, inadmissible. As a consequence, the Government's claim fails as a matter of law.

The Government's attempt to prove the value of the stock by the Stipulation entered in the tax court case involving the Estate of Birnie Davenport ignores the limiting language of the Stipulation itself. It also runs afoul of the preclusive effect of Rule 408 of the Federal Rules of Evidence. The Stipulation was clearly reached to settle that litigation; it cannot be used to prove the value of the Government's claim in this suit. *See MaHann v. Firestone Fire & Rubber Co.*, 713 F.2d 161, 166 (5th Cir. 1983).

The sale of Botefuhr's stock for $2,190.00 per share in July 1981 is a post-event transaction which is inadmissible under existing Fifth Circuit authority. *See Estate of Smith v. Commissioner,* 198 F.2d 515 (5th Cir. 1999).

The Judgment taken against Botefuhr by the Government which, by agreement, established the stock's value at $2,190.00 per share is also barred by Rule 408 and *Estate of Smith, supra*.

Finally, the Court has concluded that the newly surfaced Agreement is, despite its broad language, also inadmissible. Under Oklahoma law, when the terms of a contract are susceptible to only two reasonable constructions, the terms will be

construed against the drafter of the contract. *McMinn v. City of Oklahoma City*, 952 P.2d 517, 522 (Okla. 1997). The Government has conceded that it drafted the Agreement which, *inter alia,* values Hondo stock at $2,400.00 per share as of December 2, 1979. For the purposes of this litigation, the relevant terms of the Agreement can have only two reasonable interpretations. First, as the Government contends, the Agreement can be read to establish the per-share value of any Hondo stock and its admissibility in any proceeding involving tax liability. Or, second, as Davenport contends, it can be read to establish the value of Elizabeth Davenport's Hondo stock and be admissible only in proceedings involving tax liability wherein the basis of Elizabeth's stock is an issue. Applying Oklahoma law, the Court is bound to construe the terms in Davenport's favor. Such a construction is also consistent with the underlying reason for the agreement. The Agreement was made "for settlement" of the litigation involving the Estate of Elizabeth Davenport and as a Settlement Agreement it is inadmissible under Rule 408 to prove the value of the Hondo stock involved in this case. *See Belton v. Fibreboard Corp.*, 724 F.2d 500, 504-05 (5th Cir. 1984).

For the foregoing reasons, the Court finds that the Government has no admissible evidence to prove an essential element of its claim: the per-share value of the Hondo stock of Birnie Davenport as of July 2, 1980. It is, therefore, the ORDER of this Court that the "Third Motion for Summary Judgment"

(Instrument no. 170) of Defendant Gordon E. Davenport is GRANTED.

APPENDIX F

United States District Court, S.D. Texas,
Galveston Division.

UNITED STATES of America, Plaintiff,
v.
Gordon E. DAVENPORT, Defendant.
No. CIV.A G-03-923.

January 18, 2006.

FINAL JUDGMENT

For the reasons stated in this Court's Opinion and Order of even date herewith, it is **ORDERED** and **ADJUDGED** that Plaintiff, the United States of America, take nothing and that this action is **DISMISSED on the merits**.

THIS IS A FINAL JUDGMENT.

DONE at Galveston, Texas, this 18th day of January, 2006.

s/John R. Froeschner
John R. Froeschner
United States Magistrate Judge

APPENDIX G

United States Tax Court.
Estate of Birnie M. DAVENPORT, deceased,
Patricia L. Vestal, Personal Representative,
Petitioner
v.
COMMISSIONER OF INTERNAL REVENUE,
Respondent
Docket Nos. 22900-94, 23011-94.

August 25, 1997.

Thomas G. Potts, for petitioner.
Elizabeth Downs and *Bruce K. Meneely*, for respondent.

MEMORANDUM FINDINGS OF FACT AND OPINION

VASQUEZ, Judge:

Respondent determined the following deficiencies in, and addition to, petitioner's taxes:

Year	Gift Tax Deficiency	Estate Tax Deficiency	Addition to Tax Sec. 6651
1980	$1,422,154	-	$355,538
1991	-	$25,131	-

Unless otherwise indicated, all section references are to the Internal Revenue Code as in effect during 1980, and all Rule references are to the

Tax Court Rules of Practice and Procedure.

Respondent determined a gift tax deficiency for the estate of Birnie M. Davenport on the ground that Birnie M. Davenport (Birnie) made taxable gifts in 1980 of shares of stock in Hondo Drilling Co., Inc. (Hondo). Respondent also determined a deficiency in petitioner's estate tax due to an increase in adjusted taxable gifts made in previous years.[1]

The primary issues for decision are:

(1) Whether Birnie owned stock of Hondo during her lifetime; and if so,

(2) whether Birnie transferred stock of Hondo to Gordon Davenport, Patricia Vestal, and Charles Botefuhr in July of 1980; and if so,

(3) whether Birnie's transfer of Hondo stock in July of 1980 constituted a gift for Federal gift tax purposes;

(4) whether the 1980 Federal gift tax return filed by the Estate of Birnie M. Davenport was delinquently filed; and

(5) whether the period of limitations for assessing a

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[1] The cases involving the estate tax and the gift tax deficiencies were consolidated for purposes of trial, briefing, and opinion. The parties do not address the estate tax deficiency on brief. We assume, therefore, that the parties agree that our resolution of the gift tax issue will also resolve the estate tax deficiency.

gift tax deficiency in this case has expired.

As a preliminary matter, we must decide whether certain documents submitted by respondent during the trial of this case should be admitted into evidence. Prior to trial, petitioner submitted two motions seeking to exclude these documents from evidence. At trial, respondent sought to admit four of the documents which were, inter alia, referenced in those motions. Petitioner maintained its objections to the challenged documents at trial. The documents which are the subject of petitioner's motions and subsequent objections are:

1. An agreement executed by Patricia Vestal, Gordon Davenport, and Charles Botefuhr on November 28, 1980, which references transfers made by Birnie Davenport to Patricia Vestal, Gordon Davenport, and Charles Botefuhr (Exh. AD).

2. A letter dated April 11, 1984, from John H. Conway, Jr., Esq., and Charles B. Tetrick, Esq., addressed to Mr. Gordon Davenport and Mrs. Pat Vestal regarding the settlement of the estate of Elizabeth G. Davenport Tax Court case (Exh. AF).

3. An agreement dated April 22, 1984, involving the Commissioner and the Estate of Elizabeth G. Davenport, Deceased, Gordon E. Davenport, and Patricia Vestal, Executors (Exh. AE).

4. A letter dated August 3, 1991, from Edward Botefuhr to Corrine Childs in response to a letter from Ms. Childs requesting information on a gift tax

return that was allegedly to be filed by Mr. Botefuhr on behalf of Birnie (Exh. AG).

Petitioner argues that Exhibits AF and AE are not admissible pursuant to Federal Rules of Evidence 408 (hereinafter rule 408) and section 7121, and that Exhibits AD and AG are not admissible pursuant to this Court's standing pretrial order. Over petitioner's objection, these items were offered at trial subject to the parties' arguing their admissibility on brief.

Exhibits AF and AE

Petitioner contends that Exhibits AF and AE should be excluded from evidence pursuant to Federal Rules of Evidence 408.[2] Petitioner argues that these exhibits are inadmissible evidence of settlement negotiations. Petitioner contends that these exhibits relate to issues raised in connection with a case before this Court titled *Estate of Davenport v. Commissioner*, docket No. 26022-83. That case involved the issues of (1) ownership of shares of Hondo, and (2) the value attributable to that stock. Respondent contends that respondent does not seek to introduce the documents to prove

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[2] Fed.R.Evid. 408 provides, inter alia:
Evidence of (1) furnishing or offering or promising to furnish, or (2) accepting or offering or promising to accept, a valuable consideration in compromising or attempting to compromise a claim which was disputed as to either validity or amount, is not admissible to prove liability for or invalidity of the claim or its amount. Evidence of conduct or statements made in compromise negotiations is likewise not admissible.

liability for, validity or invalidity of, or the amount of the claim which was the subject of the parties' dispute with respect to the estate of Elizabeth Davenport. Respondent contends that Exhibit AE was introduced to show that only 1,610 shares of Hondo stock were included in the estate of Elizabeth Davenport for Federal tax purposes and that Exhibit AF was introduced to show that respondent conceded the joint ownership issue with respect to the estate of Elizabeth Davenport. Additionally, one of the fiduciaries who signed the estate tax return, and prosecuted the petition, on behalf of that estate, namely Patricia Vestal, is the personal representative of Birnie's estate.

The obvious purpose of rule 408 of the Federal Rules of Evidence is to promote settlements. Evidence of settlement negotiations or of other attempts to compromise a claim is inadmissible if offered to show liability for the claim or that the claim is invalid. Fed.R.Evid. 408; *Wentz v. Commissioner*, 105 T.C. 1, 5-6, 1995 WL 392551 (1995).

We agree with respondent that Exhibits AE and AF were not offered to show liability for any claim against the estate of Elizabeth Davenport, nor were they being offered to show the invalidity of any such claim. Consequently, we find that rule 408 does not preclude the admission of those exhibits.

Alternatively, petitioner argues that Exhibit AE should be excluded pursuant to section 7121, which provides, inter alia:

SEC. 7121(a). Authorization.-The Secretary is authorized to enter into an agreement in writing with any person relating to the liability of such person (or of the person or estate for whom he acts) in respect of any internal revenue tax for any taxable period.

Petitioner contends that Exhibit AE is a closing agreement and that under section 7121 a closing agreement is relevant to the tax liability only of the person (or estate) named in the closing agreement. Respondent fails to address this argument on either opening or reply brief.

Exhibit AE is not a closing agreement within the scope of section 7121. See *Klein v. Commissioner*, 899 F.2d 1149, 1152 (11th Cir. 1990). Accordingly, we shall deny petitioner's motion and overrule petitioner's objections to the admission of Exhibits AE and AF.

Exhibits AD and AG

Petitioner contends that Exhibits AD and AG should be excluded from evidence pursuant to this Court's standing pretrial order which reads, in relevant part:
Any documents or materials which a party expects to utilize in the event of trial (except for impeachment), but which are not stipulated, shall be identified in writing and exchanged by the parties at least 15 days before the first day of the trial session. The Court may refuse to receive in evidence any

document or material not so stipulated or exchanged, unless otherwise agreed by the parties or allowed by the Court for good cause shown.

Petitioner objected to the admission of these exhibits on the grounds that they were not exchanged prior to 15 days before trial as required by the standing pretrial order.

Petitioner first informed respondent on March 6, 1996, that it intended to argue that Birnie never owned the Hondo stock in issue. On March 11, 1996, respondent filed a trial memorandum with this Court. In the trial memorandum, respondent states that petitioner has raised a new issue regarding the decedent's ownership of the property which is the subject of the gift tax, of which respondent received notice on March 6, 1996. The new issue has not been fully articulated by the petitioner and the respondent has not had the opportunity to evaluate the argument or respond to it.

On March 21, 1996, 4 days before the calendar call which included the instant case, respondent faxed, inter alia, Exhibits AD and AG to petitioner's counsel and indicated that they should be included in a supplemental stipulation of facts. These documents relate to petitioner's new argument. Petitioner claims that respondent purposely delayed presenting these documents and that they should be excluded from evidence pursuant to the pretrial order. We disagree.

The purpose of the pretrial order is to avoid

surprise, promote stipulation of uncontroverted facts and exhibits, and shorten trial time. Respondent responded to petitioner's new argument within a reasonable time. Petitioner was presented with these documents prior to the start of the trial and had sufficient time to prepare a response. Additionally, these documents were initially provided to respondent by petitioner.[3] Fundamental fairness dictates that respondent be allowed the opportunity to offer into evidence these documents which respondent claims will refute petitioner's position. See *Moretti v. Commissioner*, 77 F.3d 637, 644 (2d Cir. 1996). Where, as in this case, a party has shown good cause for any failure to comply with this Court's standing pretrial order, we may excuse such noncompliance. Accordingly, we shall overrule petitioner's objection to the admission of Exhibits AD and AG and deny petitioner's motion in opposition to admission of documentary evidence as it relates to those exhibits.

FINDINGS OF FACT

Some of the facts have been stipulated and are so found. The stipulation of facts and attached exhibits are incorporated herein by this reference. At the time the instant petitions were filed, Patricia L. Vestal, the personal representative of the Estate of Birnie M. Davenport, resided in Tulsa, Oklahoma.

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[3] Respondent argues on brief that these documents were originally provided by petitioner, and petitioner does not dispute this on reply brief. We therefore conclude that these documents were provided by petitioner.

Birnie, decedent, died at the age of 85 on February 6, 1991, in Tulsa, Oklahoma. Decedent died testate. Decedent's last will and testament was admitted to probate on April 4, 1991. Patricia L. Vestal, decedent's niece, and Gordon E. Davenport and Charles E. Botefuhr, decedent's nephews, were appointed by the probate court to act as co-personal representatives of the estate of Birnie M. Davenport. A Form 706 United States Estate Tax Return for the Estate of Birnie M. Davenport was filed timely on November 7, 1991. The estate tax return filed on behalf of petitioner was signed by Patricia L. Vestal and Gordon E. Davenport as co-personal representatives of the estate. The estate tax return showed tax due of $144,030, which was paid at the time the return was filed.

A Form 709, United States Quarterly Gift Tax Return for 1980 (1980 gift tax return), was filed on behalf of Birnie simultaneously with the estate tax return, on November 7, 1991. The 1980 gift tax return was signed by Patricia L. Vestal and Gordon E. Davenport. The 1980 gift tax return reflected a gift of 537 shares of Hondo stock made on July 7, 1980, by Birnie to Charles Botefuhr. For purposes of computation of the 1980 gift tax, the estate valued the 537 shares of Hondo stock at $804 per share. The 1980 gift tax return reflected a gift tax due in the amount of $95,322, which was paid at the time that the return was filed.

Birnie lived most of her adult life with her older sister, Elizabeth Davenport (Elizabeth). Both

Birnie and Elizabeth remained unmarried and pursued careers with oil and gas companies-Birnie as a legal secretary and Elizabeth as an assistant to senior corporate executives. Both Birnie and Elizabeth had extensive business experience.

Pursuant to an oral agreement[4] of at least 30 years prior to the death of Elizabeth, Birnie and Elizabeth commingled all of their earnings and assets. Birnie and Elizabeth maintained joint checking and savings accounts. Birnie and Elizabeth built a home together, sharing equally in the costs of construction and maintenance. Title to the sisters' house was held in both of their names. Pursuant to the sisters' oral agreement, legal title to shared assets was held in Elizabeth's name. Birnie and Elizabeth shared the costs of all investments and considered all investments to be equally and jointly owned. The sisters' shared assets included all stocks and bonds held in the name of Elizabeth.

Birnie and Elizabeth both participated in making investment decisions and agreed that each of them owned one-half of all property acquired by them regardless of the name in which title was held. These assets included 3,220 shares of stock of Hondo. Birnie considered 1,610 shares of the Hondo stock her own property notwithstanding that the shares were held in Elizabeth's name.

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[4] Petitioner asserts that this oral agreement created a business partnership between the two sisters. We shall address this assertion in our discussion; for convenience, however, in our findings of fact we shall refer to it as either the agreement or the arrangement.

Birnie prepared the Federal and State income tax returns for both herself and Elizabeth until 1965. In accordance with their joint ownership agreement, on the Federal and State income tax returns which Birnie prepared for herself and her sister, Birnie reported one-half of all investment income as being hers and one-half as being Elizabeth's.

Birnie and Elizabeth maintained an office in their home from which they conducted their investment activities. Birnie reported one-half of the allowable deductions with respect to such office on her own Federal income tax returns and one-half on Elizabeth's Federal income tax returns. After 1965, the Federal and State income tax returns of Birnie and Elizabeth were prepared by Corrine Childs, C.P.A., a licensed attorney, tax adviser, and tax return preparer. Birnie and Elizabeth informed Ms. Childs of their joint ownership agreement and of the manner in which they had been reporting their income, deductions, gains, and losses with respect to their investments. On the returns which Ms. Childs subsequently prepared for Birnie and Elizabeth, income, deductions, gains, and losses with respect to investments were reported one-half on the return of Birnie and one-half on the return of Elizabeth.

Throughout the period of their agreement, Birnie and Elizabeth filed their Federal and State income tax returns reporting their wage earnings separately and sharing equally in the profits and losses resulting from their various investments. Several of the Federal income tax returns filed by

Birnie and Elizabeth during the period 1965 through 1979 were audited. Upon explanation of the joint ownership arrangement between the sisters, their split of investment income and expenses and reporting of 50 percent of said income and expenses on each of their returns was accepted by the Internal Revenue Service (IRS).

Elizabeth died on December 2, 1979. Gordon Davenport and Patricia Vestal were appointed the coexecutors of Elizabeth's estate. Charles Botefuhr also was appointed a coexecutor of the estate of Elizabeth Davenport. Mr. Botefuhr resigned as a coexecutor of Elizabeth's estate in September, 1980, over a dispute on how to report assets titled in Elizabeth's name.

The estate of Elizabeth Davenport filed Federal and State estate tax returns which included one-half of the value of the stocks and bonds, the legal title to which was held in Elizabeth's name at the time of her death, in Elizabeth's gross estate. These stocks included 1,610 shares of Hondo stock, valued at $804 per share. The remaining one-half of the stock of Hondo was considered by the coexecutors of Elizabeth's estate to be Birnie's property pursuant to the sisters' oral agreement.

The Federal estate tax return for the Estate of Elizabeth Davenport was prepared by Ms. Childs and was signed and filed by Patricia Vestal and Gordon Davenport. The estate tax return for the Estate of Elizabeth Davenport was examined by the IRS. The IRS took the position that the entire value

of all assets held in Elizabeth's name should be included in her gross estate, and that the 3,220 shares of Hondo stock should be valued at $3,019 per share. The IRS issued a notice of deficiency, and the estate of Elizabeth Davenport petitioned this Court. That case was captioned Estate of Davenport v. Commissioner, docket No. 26022-83. For purposes of the Tax Court litigation, the estate of Elizabeth Davenport was represented by Patricia Vestal and Gordon Davenport. Elizabeth's Federal estate tax case was settled by the parties without trial, and an agreed decision was entered on May 24, 1984.

An agreement was signed by Gordon Davenport on April 18, 1984, and by Patricia Vestal on April 22, 1984, in which the basis of the settlement agreement with regard to stock of Hondo was set forth. In settling the case, the parties agreed that 1,610 shares of Hondo stock would be included in the gross estate of Elizabeth at a value of $2,400 per share. The Commissioner conceded the ownership issue, recognizing the split of ownership of assets by Elizabeth and Birnie.

Birnie's last will and testament was drafted by Ms. Childs and was executed by Birnie on January 26, 1970. Elizabeth's last will and testament was drafted by Ms. Childs and was executed by Elizabeth on January 26, 1970. The sisters' wills contained mirror provisions. Both wills contained provisions for the distribution of each sister's respective interest in Hondo stock. The provision for distribution of Hondo stock in each of the sisters' wills was consistent with their joint

ownership agreement.

Birnie, Elizabeth, and Ms. Childs knew at all times relevant to this case that Elizabeth was the nominal owner of the 3,220 shares of stock of Hondo. Patricia Vestal, Gordon Davenport, and Charles Botefuhr also knew at all times relevant to this case, from at least the date of Elizabeth's death, that Elizabeth was the nominal owner of 3,220 shares of Hondo stock.

Upon the death of Elizabeth in December 1979, the district court of Tulsa County undertook the probate of her estate. As part of the probate of Elizabeth's estate, the court investigated the validity of the joint ownership of property by Elizabeth and Birnie. On February 14, 1983, the district court of Tulsa County determined that while Elizabeth was the record owner of certain real and personal property, she owned only an undivided 50-percent interest in such property, and held an undivided 50-percent interest in such property for her sister Birnie.[5] The district court of Tulsa County determined that each sister owned an undivided 50-percent interest in real and personal properties

[5] Petitioner, objecting to this finding of fact, states on brief that "This Order, along with an affidavit signed by Birnie M. Davenport, were both obtained to influence the then pending Protest and subsequent Tax Court case involving the Estate of Elizabeth G. Davenport with Respondent's predecessor." We assume that petitioner is implying that, in her affidavit, Birnie misstated the facts or omitted relevant facts which caused the court to reach an incorrect conclusion. Petitioner's objection is unfounded.

described in the attachment to its order. The district court found that Elizabeth and Birnie each owned an undivided 50-percent interest in the 3,220 shares of Hondo stock. The court ordered, on February 14, 1983, that the coexecutors of Elizabeth's estate were to assign and convey to Birnie her 50-percent interest in the described real and personal property.

In 1980, shortly after Elizabeth died, Birnie decided to transfer all of her 1,610 shares of Hondo stock, in approximately equal portions to her niece and two nephews. In order to transfer, among other items, the Hondo stock, Birnie entered into sales agreements with both Patricia Vestal and Gordon Davenport on July 2, 1980. The sales agreements were dated July 2, 1980, but were executed by Birnie on September 26, 1980. Pursuant to the sales agreements, Birnie sold 537 and 536 shares of Hondo stock to Gordon Davenport and Patricia Vestal, respectively. As part of the sales agreements, Birnie, as seller, represented and covenanted that she was the sole owner of and had the right to sell all the shares of stock referred to in the sales agreements. In the sales agreements, Birnie, as seller, stated that the shares of stock referred to in the agreements were not to be disposed of except pursuant to the terms of the agreements. In the sales agreements, Birnie promised to deliver good and marketable title to the shares of stock referred to in the sales agreements. By the terms of the sales agreements, Birnie transferred to Patricia Vestal and Gordon Davenport the right to receive dividends paid after the date of the agreements with respect to the shares of stock transferred and the

right to vote the stock covered by the sales agreements. In consideration for the transfer of stock to them by Birnie, Gordon Davenport and Patricia Vestal executed installment notes, dated July 2, 1980, in the amounts of $449,175.50 and $448,353.50, respectively.[6] Patricia Vestal and Gordon Davenport each made downpayments in the amount of $1,000 to Birnie with respect to the transfer to them of Hondo stock and other stock, pursuant to the sales agreements and notes. Patricia Vestal and Gordon Davenport made interest payments due from them to Birnie under the terms of the sales agreement and installment notes until approximately March of 1982. On March 5, 1982, Birnie forgave the debts of Patricia Vestal and Gordon Davenport owed to her under the installment notes. On March 31, 1983, Birnie filed a Federal gift tax return for 1982 reflecting the forgiveness of the installment notes.

On July 7, 1980, Birnie executed a document titled Deed of Gift, memorializing her gift of 537 shares of Hondo stock to her nephew Charles Botefuhr. The deed of gift was made part of the public record by filing it in Tulsa County, Oklahoma. After the date of Elizabeth's death, but prior to July 1980, dividends paid with respect to Birnie's 1,610 shares of Hondo stock were paid out of Elizabeth's estate to Birnie. The payment of dividends with respect to Birnie's 1,610 shares of Hondo stock was not considered to be a distribution of property of

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[6] This represents a purchase price of $804 per share for the Hondo stock.

Elizabeth's estate, as these dividends were considered to be Birnie's property, pursuant to the sisters' joint ownership agreement. Birnie reported the receipt of dividends paid in 1980, prior to July 1980, with respect to the 1,610 shares of Hondo stock on her 1980 Federal income tax return. After July of 1980, and before April of 1981, dividends paid with respect to the 1,610 shares of Hondo stock transferred by Birnie to her niece and two nephews were paid out of Elizabeth's estate directly to Patricia Vestal, Gordon Davenport, and Charles Botefuhr, in proportion to the stock they had received pursuant to the sales agreements and gift. Hondo typically paid dividends on or about March 1 of each year, in May of each year, and on or about August 31 of each year. The record ownership of 1,610 shares of Hondo stock was transferred on the stock ledger of Hondo from the name of Elizabeth Davenport to the names of Patricia Vestal (536 shares), Gordon Davenport (537 shares), and Charles Botefuhr (537 shares), on April 14, 1981. This transfer of ownership on Hondo's stock ledger of the 1,610 shares of stock was made pursuant to the direction of Gordon Davenport and Patricia Vestal. The transfer of title to the 1,610 shares of Hondo stock, 536 shares to Patricia Vestal, and 537 shares each to Gordon Davenport and Charles Botefuhr, was made to accomplish Birnie's intentions, and to complete the transfers made by the sales agreements and Deed of Gift. Patricia Vestal, Gordon Davenport, and Charles Botefuhr received their interests in stock of Hondo from Birnie in July of 1980.

On November 28, 1980, Patricia Vestal,

Gordon Davenport, and Charles Botefuhr executed an agreement. In the agreement it was recited that Charles Botefuhr had been given 537 shares of Hondo stock by instrument dated July 7, 1980, executed by Birnie Davenport. In the agreement it was recited that Charles Botefuhr had agreed with Birnie at the time of the gift of stock that he would file the requisite Federal and State gift tax returns and pay all taxes. Pursuant to the agreement, Charles Botefuhr agreed with Gordon Davenport and Patricia Vestal that he would file the gift tax returns with respect to the gift of July 7, 1980, and pay any gift taxes due with respect to the gift. Charles Botefuhr did not file any gift tax returns on behalf of Birnie.

Charles Botefuhr redeemed his 537 shares of Hondo stock on July 15, 1981, for $2,190 per share. Prior to redeeming his stock, Charles Botefuhr received dividends in 1981 with respect to his 537 shares of Hondo stock in the amount of $8,055. Gordon Davenport received dividends in 1981 with respect to his 537 shares of Hondo stock in the amount of $16,110.

While preparing Birnie's estate's tax returns, Ms. Childs discovered that no Federal gift tax return had been filed with respect to the Hondo stock transfer to Charles Botefuhr on July 7, 1980. She then prepared a gift tax return with respect to the transaction and filed it simultaneously with the Federal estate tax return for Birnie's estate.

Elizabeth, Birnie, their estates, and the

representatives of their estates, consistently represented to the IRS that Elizabeth and Birnie were joint and equal owners of various property, including Hondo stock, title to which was in Elizabeth's name.

Hondo stock was valued for all purposes by Elizabeth and her estate, Birnie and her estate, Patricia Vestal, and Gordon Davenport, at $804 per share. The $804 price of Hondo stock was determined by reference to the financial statement of Hondo of the price it would pay for redemptions of its stock in the fiscal year September 1, 1979, through August 31, 1980.[7]

The statutory notices of deficiency, on which this case is based, were mailed to petitioner on September 20, 1994.

OPINION

Petitioner's primary argument is as follows: Elizabeth and Birnie entered into a "business partnership" in which legal title to all of the partnership's assets was held in Elizabeth's name; following Elizabeth's death in 1979, Birnie failed to exercise her statutory rights as surviving partner to wind up the affairs of the business partnership and to distribute the assets of the partnership to the estate of her sister and herself; and finally, that

[7] For purposes of this case, if we find that Birnie did transfer the stock in question, the parties have stipulated the fair market value of such stock was $2,000 per share at the time of the transfer.

Birnie's failure to exercise her statutory rights operated as a waiver of her rights which allowed the partnership property to remain in Elizabeth's name subject to distribution by her executors in accordance with the terms of her will.

Agreement Between Birnie and Elizabeth

Respondent contends that no business partnership was formed and that the assets that the sisters acquired were merely personal assets which Birnie and Elizabeth jointly owned. Petitioner argues that because the sisters created a business partnership, Birnie's actions (or inaction) subsequent to Elizabeth's death resulted in the partnership's assets being left in Elizabeth's name and thus being disposed of through Elizabeth's estate with the consequence that Birnie did not have a sufficient interest in the Hondo stock to make a gift of that stock.

Section 301.7701-1(c), Proced. & Admin. Regs., provides, in pertinent part, as follows:

Although it is the Internal Revenue Code rather than local law which establishes the tests or standards which will be applied in determining the classification in which an organization belongs, local law governs in determining whether the legal relationships which have been established in the formation of an organization are such that the standards are met. Thus, it is local law which must be applied in determining such matters as the legal relationships of the members of the organization

among themselves and with the public at large, and the interests of the members of the organization in its assets.

Because this dispute revolves around the property rights that each sister would have if the agreement created a partnership, we must look to Oklahoma State law to see if a partnership was created, and, if so, the consequences of such a classification.

In determining State law we will follow the decisions of the highest State court, but in the absence of a decision by that court, we may look to the State's lower courts' rulings and holdings. *Commissioner v. Estate of Bosch*, 387 U.S. 456, 465, 87 S.Ct. 1776, 18 L.Ed.2d 886 (1967). The burden of proof lies with petitioner. Rule 142(a). Additionally, under Oklahoma law, the burden of proving the existence of a partnership lies with the party which is attempting to rely on its existence-petitioner in this case. *Byrd v. Byrd*, 199 Okla. 663, 189 P.2d 927, 928 (Okla. 1948). "Partnership is a creature of voluntary agreement. A partnership relationship can be created by oral agreement but proof of the fact of partnership and its terms must be established, by 'clear, unequivocal and decisive' evidence. Oral testimony offered to prove these facts is not given much weight." *Singer v. Singer*, 634 P.2d 766, 770 (Okla. Ct. app.1981) (fn.refs.omitted). A partnership is created by persons "for the purpose of carrying on a trade, business, or profession". *United States v. Neel*, 235 F.2d 395, 399 (10th Cir. 1956). Of primary importance in determining the

existence of a partnership, given all of the facts and circumstances, is whether the parties, in good faith and with a business purpose, intended to form a partnership. *Commissioner v. Culbertson*, 337 U.S. 733 (1949).

We find that Elizabeth and Birnie did not intend to form a partnership but intended to share their incomes and property much as a married couple might. References to a business partnership in certain documents as well as in some of the testimony presented at trial appears to be a loose description of the sisters' arrangement rather than an attempt to define the arrangement in legal terms. We find Ms. Childs' description of the arrangement to be accurate when she stated: "They had no written articles of partnership, no written agreements, it's just the way you did things. Just as if someone in this room and I were to open an account and each put $5,000 in it and decide to invest it, we would just rock along and we'd each report our half of the gains and losses and that sort of thing." Elizabeth and Birnie were not engaged in a "trade, business, or profession." Although they combined their incomes into joint accounts and purchased various stocks, this merely amounted to co-ownership of the various accounts and stock. The evidence fails to support a conclusion that the sisters had a business relationship. On her 1980 Federal income tax return, Birnie reported dividends from only three companies in the amounts of $12,391, $48,300, and $1,350 and from the Estate of Elizabeth Davenport in the amount of $4,269. Additionally, on her 1980 return, Birnie only

reported long-term capital gains from the sale of three different stocks and no short-term capital gains. On the facts presented, we conclude that Birnie and Elizabeth were not in a business partnership but were merely co-owners of the 3,220 shares of Hondo stock. See *King v. Commissioner*, 89 T.C. 445, 458-459, 1987 WL 45153 (1987) (an investor is never considered to be engaged in a trade or business with respect to his investment activities).

It has long been settled in Oklahoma that joint ownership of real or personal property does not necessarily constitute a partnership. *Logan v. Oklahoma Mill Co.*, 14 Okla. 402, 79 P. 103 (Okla. 1904). Similarly, "Investment in oil and gas leases as cotenants or co-owners gives no presumption of the existence of partnership. In fact, it is presumed, in the absence of a contrary showing, such ownership is merely a cotenancy." *Singer v. Singer*, supra at 771 n. 11 (citations omitted)

Petitioner places great reliance on *Ryza v. Commissioner*, T.C. Memo. 1977-64, in which this Court found two individuals were engaged in a partnership for Federal tax purposes. Ryza is distinguishable from the instant case. First, Ryza used Federal tax principles to determine if a partnership existed; in the instant case we look to Oklahoma law because the question of whether a partnership existed is relevant to determine if Birnie had a sufficient property interest such that she could make a gift of Hondo stock. Second, even if we were to look to Federal tax cases for guidance, Ryza involved two taxpayers who conducted several

businesses (buying, repairing, and selling Volkswagens, an illegal abortion clinic, and a building company) in which they were each active participants in the business operations. In the instant case we are presented with two sisters who, through a regimen of frugal living, were able to amass a substantial amount of savings and assets. We find that Ryza is of no help in determining the existence of a partnership in this case. Elizabeth and Birnie were mere passive co-owners of property. Cf. *Vanderschraaf v. Commissioner*, T.C. Memo. 1997-306 (Partnerships did not constitute mere passive co-owners of property; partnerships entered into transactions, formed joint ventures, operated gas wells, and engaged in various other activities).[5]

The elements of a completed gift under Oklahoma law are: (1) Intention to give, (2) complete delivery, and (3) acceptance by the donee. *In re Estate of Carano*, 868 P.2d 699 (Okla. 1994); *McSpadden v. Mahoney*, 431 P.2d 432 (Okla. 1967). The sales agreements and the deed of gift as well as the testimony presented at trial convince us that Birnie intended to make full or partial gifts to her niece and nephews. After Birnie's transfers, the

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[5] Similarly, petitioner's reliance on *McCleary v. Brown*, 190 Okla. 19, 119 P.2d 830 (Okla. 1941), is misplaced. Petitioner relies on *McCleary* as authority for the proposition that a surviving partner's failure to assert his statutory right of possession to partnership property for dissolution constitutes a waiver of his rights. *McCleary*, like *Ryza v. Commissioner*, T.C. Memo. 1977-64, is distinguishable because it involves the active conduct of a business as opposed to the instant case which involves co-ownership of investments.

recipients began receiving the dividends from the Hondo stock. Based on all of the facts and circumstances presented in this case, we conclude that Birnie did intend to make present and irrevocable transfers of Hondo stock in July of 1980 to her niece and nephews. We conclude that Birnie owned a 50-percent interest in the Hondo stock in 1980. Because Birnie had a sufficient ownership interest[9] and the intent to make a gift of the Hondo stock, and there is no dispute as to any other element of a gift, we find that under Oklahoma law Birnie did make a completed gift of Hondo stock in July of 1980.

Statute of Limitations

Section 6501(a) provides generally that assessments of tax must be made within 3 years after the taxpayer files a return.

The Federal estate tax return for the Estate of Birnie Davenport was filed on November 7, 1991. A Federal gift tax return for the taxable year 1980, signed by the co-personal representatives of the Estate of Birnie Davenport, was filed on behalf of

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[9] Despite Birnie's lack of legal title, we find that her interest in the Hondo stock, like that of a tenant in common, was capable of being transferred. See *Starnes v. Miller*, 505 P.2d 180, 182-183 (Okla. 1972). Also, the fact that delivery of stock certificates was delayed did not prevent the gift from being complete in July of 1980. Birnie, through the use of the sales agreements and deed of gift, accomplished sufficient delivery to put the gift beyond her dominion and control. See *Richardson v. Commissioner*, T.C. Memo. 1984-595.

Birnie on November 7, 1991. Respondent mailed notices of deficiency regarding the estate and gift tax deficiencies on September 20, 1994. Petitioner contends that the previous ownership position of Respondent's predecessor as well as notification and subsequent acquiescence over a 12-year period by respondent following the filing of extensive income and gift tax returns by Birnie M. Davenport and her relatives allow Petitioner to assert that Respondent is under a 'duty of consistency' or is 'quasi estopped' to assert any gift or estate tax deficiency against Petitioner for gifts of Hondo stock by Birnie M. Davenport.

We disagree. The filing of the Federal estate and gift tax returns by Birnie's estate started the running of the periods of limitations on November 7, 1991. Respondent's notices of deficiency were mailed to petitioner on September 20, 1994, before the expiration of the period of limitations. We therefore find that the statute of limitations does not bar the assessment of additional estate and gift tax liabilities in this case.

Addition to Tax Under Section 6651(a)(1)

Section 6651(a)(1) imposes an addition to tax for failure to file a return on the date prescribed (determined with regard to any extension of time for filing), unless it is shown that such failure is due to reasonable cause and not due to willful neglect. The taxpayer has the burden of proof to show the addition is improper. *United States v. Boyle*, 469 U.S. 241, 245, 105 S.Ct. 687, 83 L.Ed.2d 622 (1985).

Respondent determined that a Quarterly Gift Tax Return with respect to the July 1980 gifts was due to be filed on November 15, 1980. Secs. 6019, 6075(b). Petitioner has stipulated that the co-personal representatives of Birnie's estate filed a Federal gift tax return for the quarter ended September 30, 1980, on November 7, 1991. Petitioner has made no argument with respect to the section 6651(a)(1) addition to tax, except by implication of its argument that no gift was made. We rejected that argument supra, and petitioner has not proven that its failure to file timely was due to reasonable cause. Accordingly, we sustain respondent's determination of the applicable addition to tax under section 6651(a)(1).

APPENDIX H

United States Court of Appeals
FILED
May 14, 2007
Charles R. Fulbruge, III, Clerk

IN THE UNITED STATES COURT OF APPEALS

FOR THE FIFTH CIRCUIT

No. 06-40466

UNITED STATES OF AMERICA

Plaintiff - Appellant

v.

BIRNIE DAVENPORT, ET AL

Defendants

GORDON E DAVENPORT

Defendant – Appellee

Appeal from the United States District Court
for the Southern District of Texas, Galveston

ON PETITION FOR REHEARING AND
REHEARING EN BANC

(Opinion 4/9/07, 5 Cir., _____, _____ F.3d _____)

Before KING, GARZA, and PRADO, Circuit Judges

PER CURIAM:

(**X**) The Petition for Rehearing is DENIED and no member of this panel nor judge in regular active service on the court having requested that the court be polled on Rehearing En Banc, (FED. R. APP. P. and 5TH CIR. R. 35) the Petition for Rehearing En Banc is also DENIED. The mandate shall issue forthwith.

( ) The Petition for Rehearing is DENIED and the court having been polled at the request of one of the members of the court and a majority of the judges who are in regular active service and not disqualified not having voted in favor, (FED. R. APP. P. and 5TH CIR. R. 35) the Petition for Rehearing En Banc is also DENIED.

( ) A member of the court in active service having requested a poll on the reconsideration of this cause en banc, and a majority of the judges in active service and not disqualified not having voted in favor, Rehearing En Banc is DENIED.

ENTERED FOR THE COURT:

s/Carolyn D. King
United States Circuit Judge